INTERNATIONAL LIFE UNDERWRITERS' LIBRARY

Stephenson

EX LIBRIS

GILBERT THOMAS STEPHENSON

Digitized by the Internet Archive
in 2025

https://archive.org/details/bwb_Y0-DWG-942

BUSINESS LIFE INSURANCE

THE INTERNATIONAL
LIFE UNDERWRITERS LIBRARY

ADVISORY BOARD OF EDITORS

Edward A. Woods — Graham C. Wells
Ernest J. Clark — W. Lyle Reid
Winslow Russell

AMERICA'S HUMAN WEALTH
by Edward A. Woods

BUSINESS LIFE INSURANCE by Ralph Sanborn

COMMON SENSE HEALTH
by Arthur Geiringer, M.D.

CREATING AND CONSERVING ESTATES
by E. A. Woods and A. C. Robinson

FORTY UNUSUAL PLANS FOR SELLING LIFE INSURANCE
by J. Stanley Edwards

LIFE INSURANCE AS A LIFE WORK
by Hugh D. Hart

PUBLICITY METHODS FOR LIFE UNDERWRITERS
by Arthur H. Reddall

SELLING THE SALARY INSURANCE PLAN
by Richard L. Place

IN PREPARATION

MENTAL ATTITUDE by Mansur B. Oakes

SELLING BUSINESS INSURANCE
by Charles J. Rockwell

SELLING PROGRAM INSURANCE
by James Elton Bragg

THE FINANCIAL PROBLEMS OF OLD AGE
by Albert W. Atwood

PRACTICAL LIFE INSURANCE SALESMANSHIP
by Charles J. Rockwell

WHAT EVERY POLICYHOLDER SHOULD KNOW ABOUT HIS POLICY by G. B. VanArsdall

SELLING ADVENTURES IN LIFE UNDERWRITING
by Guy MacLaughlin

The International Life Underwriters Library

BUSINESS LIFE INSURANCE

BY

RALPH SANBORN

Approved by
National Association of Life Underwriters
The Life Underwriters Association of Canada

F. S. CROFTS & CO.
NEW YORK 1927

DR. NORMAN A. WIGGINS

COPYRIGHT, 1927, BY F. S. CROFTS & CO., INC.

MANUFACTURED IN THE UNITED STATES OF AMERICA
BY THE VAIL-BALLOU PRESS, INC., BINGHAMTON, N. Y.

CONTENTS

CHAPTER		PAGE
	Introduction	7
I	Business and Life Insurance	13
II	The Elements of Proper Protection	26
	CORPORATIONS	
III	Corporations and Life Insurance	49
IV	Credit Reinforcement	55
V	Direct Compensation	67
VI	Liquidation Fund	88
	PARTNERSHIPS	
VII	Partnerships and Life Insurance	133
VIII	Credit Reinforcement	136
IX	Liquidation Fund	147
X	Direct Compensation	172
	PROPRIETORSHIPS	
XI	Proprietorships and Life Insurance	195
XII	Credit Reinforcement and Liquidation Fund	198
XIII	Purchase Plan	215
XIV	Direct Compensation	229
	CONCLUSION	
XV	Coöperation	247
	Index	263

000263

INTRODUCTION

Life insurance is an indirect outgrowth from the early marine protective groups which constituted the genesis of all forms of insurance as they are known today. The inspiration for life insurance doubtless came when men realized that society could ease the burden of a dead man's beneficiaries —if they could be called that—by distributing the risk as they had done with the insurance on a ship sailing the high seas.

The development of the actuarial and underwriting phases of life insurance has been steady, sure, and complete up to the present form in which it is issued. Of course, new benefits, new provisions, and new medical and legal opinions are continually appearing. They clamor for intelligent analysis and experience, and receive it. The public may procure policies of life insurance which will provide many forms of protection in most cases and in many ways.

However, the very obvious progress in the actuarial and underwriting phases has not been accompanied—as it should have been—by pro-

portionate progress in the application of those policies to the possible needs. It is only during the past ten years or so that scientific application of protection has been considered or practiced. Today there is an insistent desire on the part of life insurance men, and an insistent demand on the part of the public, that the new insurance shall be applied toward a definite reinforcement of some portion of the insured's estate.

During this transition, and somewhere on the way, the fundamental purpose of insurance, as used for lives, seems to have been lost. Its very reason for existence has been sloughed off. Consequently, insurance is not placed on every life as it is on almost every vessel on the sea against loss. Vessels are lost and the owners or sponsors are reimbursed. Lives are lost, but only about seven per cent of the human life values in the United States are insured against loss. The insurable interest is there, the need is there, the life should be insured.

The volume of new life insurance each year has been astounding. Each successive year, with the one exception of 1921, has been better than its predecessor. Many business men have explained this phenomenon by saying, "Great salesmanship." It seems more accurate, however, to say that com-

monsense application of all policy contracts to *definite* needs has been responsible for this growth.

Salesmanship, as such, should be developed to its greatest extent only that the life insurance underwriter by its use may thus be able to acquire the opportunity of proving his ability as a specialist in properly underwriting these needs. The liquidation of inheritance and estate taxes, the creation of trusts, the establishment of charitable bequests, the provision for special needs of each family, the amortization of mortgages are some of the needs which have led to specialization on the part of the life insurance underwriter. One of the most important special applications of life insurance is in the business world. This should be broadened to include the several professions as well. Business has just recently discovered the adaptability of life insurance to the solving of some of its financial problems. Its application as a protective measure against the loss by death of human assets is still undeveloped, but business men are less inclined than ever to be without the protection which life insurance so efficiently provides.

It is intended to include within these pages the technique of applying life insurance to everyday business needs, together with a discussion of the procedure to be followed in order to protect the

interests of the insured, the beneficiary, and the business itself. This plan is followed because of the many pitfalls that stand gaping to receive those who venture into the intricacies of a problem which lures by virtue of an illusionary simplicity. There are many phases of a complete business life insurance "case" which need the attention of a specialized knowledge. This explanation may help to point out the way which may be followed, but it is suggested that a competent life insurance underwriter should be consulted in order that the greatest good may be obtained from the effort and money expended.

View the following pages with the thought that the subject has been discussed in a technical manner. However, it has been the aim of the writer to confine the phraseology to the use of such terms as can be understood as well by the average business man as by the professionally trained life insurance underwriter. No effort has been made to submit concrete selling plans, but the book is intended rather as an answer to that frequent question, "What is the need for life insurance in a business, and what is the method of meeting it?"

Owing to the fact that this book is intended for general use by life insurance underwriters representing all life insurance companies it is obvious

that it would be impossible to give a detailed discussion of each company's requirements for business protection. Each underwriter should familiarize himself with his own company's policy forms and applications so that he may thus give his client the benefit of any service which has been adapted for the sole use of a business organization. Furthermore, it has been impossible to cite in detail the requirements of the innumerable State laws which would show considerable variation in the matter of providing correct protection for a client. Consequently, the life insurance underwriter should familiarize himself with the statutes of his own State insofar as they affect business life insurance. The first chapter includes a general discussion of business life insurance followed by a description of the basic needs and the methods for meeting them. The subsequent sections and chapters give information which applies to the particular case under consideration. Because of this arrangement, it will probably be found advisable, whenever this book is used as a reference, to review the general chapter "Business and Life Insurance" before proceeding to a detailed consideration of the case.

CHAPTER I

BUSINESS AND LIFE INSURANCE

Life insurance is applied by a business organization or by individuals within it so that there may be some financial compensation for the economic loss suffered when a vital human unit in that business dies. A life insurance company issues a policy and accepts premiums thereon, thus assuming responsibility to the extent of its contract with the insuring parties. The burden of risk has been shifted from a business which cannot well afford to bear it to a life insurance company which has been organized and chartered for that very purpose.

Life insurance, in its commonly accepted form, is hardly what the term indicates. To say that it is "insurance on lives" might seem more accurate. But, in using the term "Business Life Insurance" are we not using the words "life insurance" in a very correct sense? Is it not true that when insurance on lives is intelligently applied in a business the purpose has been and should be to assure

the perpetuation of that business—or its life—in spite of the loss suffered as a result of the death of a vital human factor?

Men may give the best part of their lives to their business. Their mental and physical vitality has been spent in its behalf so that they might provide an income for themselves and their dependents. They have also associated with each other that they might attain their objective in a manner more efficient, lucrative, and expeditious.

Affiliated in this effort there have been employees of varying responsibility and number. They have been compensated for their work, but they have given their loyalty in the firm belief that they will always have employment. Many men have witnessed the havoc that can be wrought among faithful employees when a business is terminated by failure, transfer, or amalgamation. Such conditions cannot be prevented by business life insurance except when they are caused by the death of responsible men who might have better demonstrated their sense of responsibility had they been insured. Separately or collectively, men are not justified in exposing their handiwork and all those people who have assisted in its creation to the hazards of readjustment at their death.

A tree grows to fruit-bearing proportions from

a seed and continues to flourish until blight or some other act of Fate shall destroy it. Does a farmer stand idly by and resignedly accept the destruction of his possession? Hardly! He rather anticipates disaster by availing himself of all that science can offer so that he may perpetuate the life of his source of income.

The combined effort of men cannot prevent death, but the combined effort of men can minimize the damage which may be done to their business if death strikes within it. No form of insurance can replace the sentimental associations of a dead man. His associates and dependents are forced to suffer that loss. They are not forced to suffer, however, a complete economic readjustment if forethought and anticipation have provided a compensating factor.

Business life insurance is insurance by any policy form on lives within any corporation, partnership, or proprietorship against loss at death of the economic value of that life to that business.

There are three forms of business enterprise—a corporation, a partnership, and a proprietorship. It is sufficient to say that a corporation is a business which has been incorporated by State charter and that a partnership is a group of two or more

individuals doing business under some recognized form of partnership agreement. A "proprietorship" according to the *Century Dictionary* is "the state or right of a proprietor; the condition of being a proprietor." Furthermore, it defines a "proprietor" as being "one who has a legal right or exclusive title to something; as owner: as, the proprietor of a farm or of a mill." Therefore, in this book the term "proprietor" will be used to describe the man himself, and "proprietorship" to describe his type of business organization. This third major classification, "proprietorships," includes that large field of commercial as well as professional activity which functions without resorting to the execution of a corporate charter or a partnership agreement. A "business" is the inclusive reference to any or all of the three forms of doing business which have just been described.

Under these three forms of business organization life insurance may be applied to meet any one, any two, or all three of the following specific needs: (1) credit reinforcement; (2) direct compensation; and (3) liquidation fund. Each classification is described in detail in the succeeding paragraphs. Furthermore, it is desirable to remember that in every paragraph of explanation which follows in this chapter the subject has been dis-

cussed in general. It is intended to include a mention of all questions which are common to all three forms of business organization, leaving for the subsequent chapters a discussion of the questions which relate to particular forms of business organizations and to plans for meeting the needs of that business.

Credit Reinforcement

It is generally conceded that the entire structure of a business organization is founded upon its ability to obtain credit, and this hypothesis must govern any use of life insurance. The same idea might be expressed in another way by saying that the most important consideration of life insurance in a business is its use as replacement of the economic value of human lives, which is really credit reinforcement. It is true that a corporation, in the event of a death, is not exposed to that same hazard of liquidation as is a partnership or a proprietorship. The two latter forms of business organizations are forced into liquidation by law as the result of a death. The corporation, on the other hand, is only called upon to make readjustment, because even a death cannot destroy its legal entity. In every instance it will be necessary to satisfy the claims of creditors before a partnership

can be divided among the survivors, or the assets of a proprietorship, if there are any, can be passed on to the beneficiaries. In the case of a corporation it will mean that readjustment of the credit situation will have to take place before it can function normally. Consequently, it is obvious that any life insurance which is the property of a corporation, partnership, or proprietorship, either on the basis of direct or indirect ownership, will be available to the creditors irrespective of manipulations which may intend to put these proceeds beyond their reach. No life insurance underwriter or business man should overlook this very important point, because it may be the subsequent cause of entangling litigation and the consequent suspension of all benefits intended to be provided by the protection of life insurance.

Life insurance is credit reinforcement, but it cannot be actual security or credit collateral for any obligation, except to the extent of its cash surrender values. As a reinforcement against credit, insurance may be written for the benefit of the creditor directly, or indirectly via the debtor's business, on the lives of those men responsible for the fulfilment of the credit obligation.

Any business man must be mindful of the fact that, in the circumstance just shown, life insurance

will be the efficient medium to the desired end. It meets that known need at the unknown time with a dispatch that has been warmly welcomed in every case which has matured.

Direct Compensation

If and when a policy of insurance on the life of any human asset in a business is payable entirely, and without restriction as to the use of those proceeds, to the treasury of that business as compensation for the economic loss of that asset, it is considered a policy of "direct compensation." The proceeds, in other words, constitute a discretionary fund which may be used by the business in any way deemed advisable. Ordinarily, however, it is expected that the proceeds would be used for the replacement of the life that was lost or to compensate the organization for the loss of business for which the deceased man was responsible. As each case of direct compensation is discussed, new ways of using the proceeds of a matured policy will be discovered.

In the following subdivisions of this subject there is a brief outline of the three types of individuals upon whose lives business life insurance for direct compensation should be carried.

The Valued Employee or the Expert

Both of these individuals are in the employ of the business. The valued employee, however, differs from the expert because he may be capable of filling more than one position within the organization. His value is general. The expert, on the other hand, is valuable because of his specific and highly developed knowledge of some particular phase of the business. Neither the one nor the other is participating in the profits except to the extent of salaries, bonuses, or commissions. For instance, the sales manager of a large cotton-cloth manufacturing company would be considered a valued employee in the sense of this definition provided, of course, that he was distinctly an employee. The expert in the same company might be the chemist who was responsible for the development of satisfactory dyes. The sales manager might on demand fill several capacities, but the expert is confined to his own specialized activity. Hence, there is the difference made.

The business can compute the worth of both types in dollars and cents, and it proceeds to compensate itself in the event of death for any past investment or future possibilities as represented in the minds and bodies of those employees.

Contracted Parties

Every type of business may at some time or other contract for the services of one or more individuals for the execution of some specific piece of work. The time allowed for execution may be variable, but the contracted party is not under obligations other than those specified. The continued existence of these individuals or groups of individuals is essential to the satisfactory completion of the work for which they have been contracted. Any suspension or cessation of activity because of death would mean a loss of money to the business. Hence, insurance should be carried on the lives of these contracted parties. Who should be responsible for the insurance, will be discussed in every subsequent case where such a form of protection has been recommended. Invariably the proceeds of such insurance are payable as direct compensation to the business. If there be any variation of this specification it will also be discussed in the subsequent cases.

It might be interesting to note an unusual example of this phase of direct compensation on a contracted party. Two young men were fortunate in having an older man as an intimate friend who wanted to set them up in business. He advanced

$50,000 working capital without any stipulation other than that such an amount would be payable to his estate immediately upon his death. The young men foresaw the possible embarrassment of such a situation and they obtained a $50,000 policy on the life of their benefactor payable to themselves.

Officers of a Corporation or Members of a Partnership

Corporation officers or partnership members invariably represent a computable worth to their business for which in the event of their loss through death, the business should receive direct compensation. In many ways their position in regard to this type of protection is quite comparable to the case of the valued employee or the expert. The business in each instance has made an investment in these men so that future return might be expected from that investment. Any interference by death with the possibility of receiving a satisfactory return should be prevented by the business if possible. Insurance on the lives of these corporation officers or partners is intended to protect the business against economic loss in such an eventuality. Proprietorships are not interested in direct compensation in this way, and

this fact will be explained by reviewing the aspects of the entire life insurance problem of proprietorships as given in a subsequent chapter.

Liquidation Fund

Life insurance may be used to provide a sum of money which shall liquidate in part or in full the interest which the deceased may have owned in the corporation, partnership, or proprietorship. This is presumably accomplished by the execution of a written agreement or understanding between the interested parties.

(a) In a corporation such an agreement is voluntary and at the discretion of the participants.

(b) In most partnerships and in most states the death of a partner necessitates dissolution and some form of liquidation of the deceased partner's interest *must* be provided.

(c) In a proprietorship such a liquidation fund might be carried on the life of the proprietor in favor of his chosen successor, with either one being the premium payer for the policy.

An outline of the uses of business life insurance, based on the preceding paragraphs of explanation, appears as follows:—

A. Corporation
   1. Credit reinforcement
   2. Direct compensation
      a. The valued employee or the expert
      b. Contracted parties
      c. Officers of the corporation
   3. Liquidation fund

B. Partnerships
   1. Credit reinforcement
   2. Liquidation fund
   3. Direct compensation
      a. The valued employee or the expert
      b. Contracted parties
      c. Partners

C. Proprietorships
   1. Credit reinforcement and liquidation fund
   2. Purchase plan
   3. Direct compensation
      a. The valued employee or the expert
      b. Contracted parties

Thus, it may be seen that there are six fundamental needs for life insurance in a corporation, that there are six in a partnership, and that there are five in a proprietorship. It will also be noticed that there is a need entitled "Purchase plan" un-

der "Proprietorships" which is not common to "Corporations" or "Partnerships." The explanation and discussion of this need will be found in the chapter entitled "Proprietorships and Life Insurance."

CHAPTER II

THE ELEMENTS OF PROPER PROTECTION

It is now necessary to discuss the general methods of applying business life insurance to meet each one of these seventeen separate needs. Such a discussion includes a consideration of the necessary amount of protection, the proper form of policy to be used, the selection of the premium payer and how to pay, how the beneficiaries should be nominated, when and how to use assignments and what they are, when and how to use supplementary agreements, when and how to use trustees in settling a case, the ownership and status of cash values and dividends, and the effect of taxation upon premium payments and proceeds at maturity.

It is desirable in reading the following paragraphs to remember that they include only such information under each heading as is common to every need. The complete process of meeting each need is discussed in separate chapters. This separation of general from specific data has been made

to minimize inevitable repetition. Nevertheless, in some instances, previous statements have been intentionally repeated so that each topic might be complete in itself, thus eliminating cross reference and page juggling.

Amount of Protection

If life insurance is to be applied for, it is because a need is existent which can best be protected by that medium. And that need can invariably be reckoned with a fair degree of accuracy. To say that one formula can be used in all cases is ridiculous. But, if there be anything which even approaches such a thing as a definite formula, it is the statement that only with just and equitable coöperation on the part of the life underwriter and the client can the amount of protection be determined. Time, of course, is going to alter circumstances. The need for added protection in later years must be considered because the insurer may be confronted with obstacles which might render the insurance plan obsolete.

An intelligent analysis of balance sheets, statements of condition, and earning reports will reveal much that will indicate the proper amount of protection required. At this point it is desirable to emphasize the importance of properly estimat-

ing the factor of good will. Many business statements carry such an item under "Assets." To what factor does good will owe its existence? Is it real good will backed up by a negotiable value or is it soft padding at the bottom of the asset column? In either case, it should be admitted as *prima facie* evidence of part of the amount of protection which is necessary. Nothing is likely to disappear more rapidly from the assets of a business than good will when death removes the man or men responsible for its existence. The amount of protection should be considered separately for every need. It is a mistake to bulk the estimate of the various needs because the inevitable result will be inadequate insurance. Of course, the opposite extreme —"over-insurance"—should be avoided with equal diligence. The needs of the clients must be protected, but only in direct ratio to their ability to pay premiums.

Policy Form

There are five fundamental policy forms which can be used as the contracts for business life insurance—ordinary, limited payment, endowment, term, and modified life. Ordinary life insurance is first on this list as it is the most important and the most used of all forms. It requires the lowest

premium of the permanent forms, and, over a period of years, shows a low net cost. In business this is a factor of considerable importance. Limited payment life insurance will very seldom be used by a business except in those rare instances when a business wishes to pay for its insurance over a period of excessive income. The advantages of this form seem to be confined to the consideration just stated plus the fact that limited payment does carry higher cash values if a business should care to avail itself of such a reserve or "silent asset." Off-setting these small advantages is the disadvantage of the much higher premium for the same protection. The use of endowment life insurance is solely confined to those cases in which a business wishes to meet a known obligation at a definite time, or upon the death of the insured individual before that time. Term insurance should only be used when the need for protection will definitely disappear in five years or less. The ordinary life contract of almost any company will show a better net cost than term insurance for a period of five years or over. This is even including the interest which the premium payer may receive for the difference in premiums. No underwriter should permit his client to overlook this fact. Modified life insurance, whether it be known

as such or by some other name, is a combination of term and ordinary life insurance. It is most desirable in cases where the term of protection may be short but with every possibility of its being continued or renewed. Attention should be called to the fact that some companies issue a so-called "corporation" policy form, and the clients should be given the benefit of this special contract when it is applicable.

Premium Payment

First and foremost under this heading comes the statement—a new policy is not in force until the first premium has been paid! In arranging for premium payments all parties should be protected. Have the best interests of the insurer and the premium payer been observed? The legal entanglements resulting from haphazard methods of premium payment are emphasized later. At this point the caution is voiced that premium payment should not be made in any way so that it seems to accomplish some minor present gain only to defeat ultimately the very purpose of the entire plan. Premiums on business life insurance should be paid annually. The premium payer should be shown the actual interest charge for paying other

than annually, as a business can invariably borrow money at a lower rate.

Beneficiaries

The beneficiary in a case of business life insurance should be so nominated that he or she will receive the policy proceeds in the manner intended and with the restrictions agreed upon. In this way it will be possible for the beneficiary in turn to distribute the money in the manner previously determined. If there is a desire to name an individual as beneficiary who has not been directly affiliated with the business it would be well to determine any legal objections to such a procedure. It should be remembered that the business interest may not be transferred directly to a beneficiary upon the death of the original holder. The executor or administrator of the estate may be a person or persons other than the ultimate beneficiary, and such an interest is first transferred to his control. If, for instance, a stockholder of a corporation wishes his wife to have control of his interest in the business the most efficient way to accomplish that end is to transfer the stock entirely to her name prior to his death. This point should be discussed with the attorneys

for the business organization in order to make absolutely sure of the execution of the original intention. Furthermore, even if there are no legal objections to the naming of an individual beneficiary outside of the business there still may be a sentimental objection. All post-mortem transactions should be executed without the influence of intimate acquaintance with circumstances which might militate against the welfare of all concerned. In this connection a trusteeship offers a splendid solution for removing the personal or sentimental factor. If a trustee is to be the beneficiary, the clause stating that nomination should be so drawn that it will include a statement of the right of that trustee to act as beneficiary—"So and So, Trustee, under instrument of trust, dated . . ." Special attention should be given to the fact that the nomination of a beneficiary and the execution of a business life insurance agreement run hand in hand, and the execution of each must comply with the specifications of the other. There should be complete coöperation between the life insurance underwriter and his clients in preparing an efficient distribution of the policy proceeds when they become a claim at death, and all legal aspects of such a transaction should be verified by the attorney for the business. Furthermore, the life in-

surance underwriter should be mindful of the fact that his home office reserves the right to pass upon the insurable interest, and where there is a question of doubt the nomination of a beneficiary should not be recommended to a client until the insuring company has had an opportunity to pass upon this point. Some companies issue policy contracts containing "secondary" or "special" beneficiary clauses for use in a business life insurance case. In general these make provision for the direct transfer of the business interest to the beneficiary even though the insurance may not be carried by the insured, and it is expected that each life insurance underwriter will be familiar with the requirements of his own company.

Assignments

The two important forms of assignment which are used in the transfer of right and title under a policy of life insurance are "collateral" and "absolute." The former is an assignment by which the assignor conveys to the assignee such right and title in the policy as may be necessary to protect the interest of the assignee in the life of the assignor. Such a relation is commonly expressed by the words "insofar as the assignee's interests may

appear in the life of the assignor." The absolute assignment conveys all right and title under the policy without qualification or reservation from the assignor to the assignee. An assignment can be a very vicious or a very effective instrument. It is often desirable, in the interests of a client, that the life insurance company review an assignment of the policy before it becomes effective. Possible embarrassment is thus averted. In connection with these recommendations it may be observed that rights and title under a policy may well amount to thousands of dollars and such amounts should not be handled carelessly. Every life insurance underwriter is always acting in the best interests of the assignor if he makes it his business to have the assignment removed immediately upon the fulfilment of the assignor's obligation to the assignee. This is necessary because it is not the general practice of life insurance companies to restrict or define the period of assignment. The assignor should naturally keep the underwriter posted as to the current status of the policy. In general, it may be said that the transfer of the rights under a policy by use of assignments is an ideal method of securing for all parties a certain execution of their wishes.

Agreements

Any discussion of the subject of agreements should be prefaced by a note of warning. The attorney for the corporation, partnership, or proprietorship should be responsible for the execution of any supplementary life insurance agreements. He knows the law, and it is his function. The life insurance underwriter may assist and he may offer suggestions. The legal department at his home office may be willing to collaborate but inasmuch as this department cannot assume any responsibility for the satisfactory execution of the agreement it is confined to acting in an advisory capacity only. Furthermore, all interested parties should be sure that the provisions of the suggested agreement in no way conflict with the statutes of the State where the parties to the agreement are doing business. Specimen agreements can be submitted by the life insurance underwriter, but only in order that the form and general provisions may be used as a guide in preparing the final agreement for the client. Any such specimen forms as appear in this book should be used only in this way. The general provisions which shall appear in an agreement are naturally dependent upon the end which

is to be attained in each case. There is one general suggestion which might be offered and which has not frequently been used. Insert a bonding clause such as the one appearing in paragraph two in the agreement on page 100. When the subject of agreements is discussed in the following pages it will be noticed that an attempt has been made to cite such distinctive attributes as are peculiar to each case and, where possible, at least one specimen agreement has been supplied. Agreements should always be used if the beneficiary stated in the policy is to execute some predetermined and prescribed transactions with the proceeds. A "business will" and a "business agreement" are synonymous. The former is, however, sometimes a more accurate term but for the sake of uniformity the name "business agreement" has been used here. The chief recommendation for a business agreement, stating it as succinctly as possible, is to say "put it in writing—verbal instructions don't go!"

Trusts

The trust departments of national banks and trust companies have recently sensed the mammoth opportunity to enlarge their service as em-

bodied in the settlement or distribution of life insurance proceeds on a prearranged basis. Their attention has been principally focused upon the creation and maintenance of personal trusts, as such funds demand a more lasting supervision. The real desirability of using a trustee to distribute business life insurance proceeds has not been emphasized. Indeed, it has hardly been recognized. The most substantial argument in favor of using a trustee when possible, has already been mentioned. Under the heading of "Beneficiaries" on page 31 it will be noticed that the use of a trustee is recommended because it is thus possible to eliminate the personal element in post-mortem transactions. However, this is only stating the case briefly and a more detailed explanation is necessary. The benefits of a trustee are numerous, whether that trustee be a commercial organization created to do that work or whether it be an individual qualified to act as such. First, there is the advantage, as stated, of personality in all transactions. Second, the trustee will and must show an impartiality toward all interests. The trustee is obliged to execute all transfers and transactions with due consideration for the rights of all. Third, the trustee can invariably comply with his instructions with greater dispatch than the individuals or

the business operating for themselves. Fourth, the use of a trustee creates one more source of valuable assistance and advice for the business. This advantage refers primarily to such help as the trust officer or trustee may give along the lines of his own activity. Lastly, the infinitesimal expense for such service classifies it as a business opportunity. There is much to be said in favor of the commercial trustee or trust officer as against the individual trustee. In the first place, one man might be incapacitated just at the wrong moment and if he alone were the trustee it would be very embarrassing. On the whole it is quite evident that the old-fashioned trustee or estate manager is disappearing and his work is being done by large trust companies and by the trust departments of the national banks. In general it may be stated that a trustee should be appointed when there is to be some special distribution of the policy proceeds and when at the same time it is undesirable for any of the principals to participate personally in that distribution. Trusts are especially useful for corporations and partnerships in liquidating a stockholder's or partner's interest by using life insurance proceeds. These uses of trusts and trustees will be discussed in more detail in later

paragraphs. Before becoming involved both the client and the life insurance underwriter should submit the problem for analysis to competent trustees in whom the client has faith. In addition, if and when a trustee is appointed, it is well to remember that the trustee then becomes the beneficiary and for that reason the insuring company must know why it is instructed to pay policy proceeds to that beneficiary. In other words, "What is the insurable interest?" And the answer is, "The instrument of trust," whereupon the insurance company will usually retaliate with, "Let's see a copy of it." For this reason complications might be avoided if all parties were to be sure that a life insurance company will accept the "insurable interest" as represented by the deed of trust which has been recommended.

Cash Values

These are the reserves accumulated against the permanent policy forms such as ordinary life, limited payment life, modified life, and endowment. They may be considered as liquid assets of the party or parties holding all right and title under the policy. They are not assets in this sense

of the word if the beneficiary clause in the policy is irrevocable without other assignment of interest. This is so because under an irrevocable beneficiary clause neither the insured nor the beneficiary can touch the cash values without the consent of the other. Thus the values are in suspension unless one party executes a release of his right to them, and by so doing he automatically voids the status of the nomination. In some cases business life insurance has been applied by virtue of the advantage accruing from enlarging this source of liquid reserve. But, by and large, it is safe to say that policyholders and life insurance underwriters should avoid undue emphasis on this point. Cash values should only be considered as an emergency fund because as such they may often prove to be a veritable business life saver. If at any time a policyholder wishes to avail himself or itself of the cash values it is wise to consult the underwriter of that policy before proceeding independently. Many misunderstandings can thus be avoided. Incidentally, it might be mentioned that under the various paragraphs entitled "Cash Values" on subsequent pages more detailed information is supplied as to ownership and use of this reserve in specific instances.

Taxation

It would be impossible, within the limits of these pages, to cite all the numerous rulings under Federal and State tax laws which might affect business life insurance transactions. Also, it would be impracticable to attempt to include detailed information on particular tax questions, for rulings and practices are constantly changing. Since the tax problem looms so high in importance in many business insurance cases, a few general statements will be ventured but the underwriter who is offering information on taxes to his clients should make sure that this information is in accord with the law in force at the time he wishes to use it.

Every life underwriter who is working on business life insurance cases should familiarize himself with the sections in the Federal tax laws and the tax laws of his own State which refer specifically to insurance. Even though his information is entirely accurate, however, it is well for him to qualify his statements to clients by saying, "That is the tax situation as it stands today. Tomorrow things may be vastly different."

Many questions are bound to arise, too, which are not covered by specific rulings. If possible, in a

situation of this kind, it is well to obtain the opinion of the tax authorities, but, since the tax authorities so often are not willing to rule on a hypothetical case, the underwriter can, if he thinks best, suggest that the business organization refer the matter to its own attorneys. If, however, the life insurance man presents his own opinion, he should be very careful to say, "That is merely my interpretation of the law. It may not represent the views which the tax authorities will take so please do not accept my ideas as final."

Although the subject of beneficiaries has been discussed elsewhere, possibly a few observations should be made here in regard to the naming of beneficiaries or the use of certain beneficiary clauses in business insurance transactions purely for the purpose of avoiding taxation. Such procedure, in the end, usually proves to be a case of "Penny wise and pound foolish." The entire life insurance plan may go awry if the policy is made payable to this or that beneficiary merely because the plan apparently provides relief from an undesirable impost. In the last analysis, the safe plan is to recommend the way in which the contract could be carried through most efficiently, the question of taxation being given secondary consideration.

Under the present (1926) Federal income tax law, *premiums paid by a taxpayer upon a life insurance policy from which the taxpayer derives any direct or indirect benefit are not deductible as a business expense.* In certain circumstances, which will be discussed in subsequent chapters, the Federal tax authorities may hold that the taxpayer derives no benefit from the policy and the deduction of premium may be allowed, but the life underwriter should be very sure of his facts before informing his client that the case is an exception to the general rule that premiums on business life insurance policies cannot be deducted in making Federal income tax returns.

On the other hand, the proceeds of policies paid at the death of the insured need not be reported as income in making Federal income tax reports (except in case of a transfer for a valuable consideration). If an endowment policy is paid during the life of the insured, or if a policy is surrendered before it matures by death, any amount received in excess of the net amount paid by the business organization for the policy is subject to Federal income tax.

Dividends payable under a participating policy are not subject to Federal income tax unless, of course, during the insured's lifetime an amount

is received in excess of the amount paid for the policy.

Insurance payable to the insured's estate must be included in his gross estate under the Federal estate tax law. An exemption of $40,000 is allowed by the Federal Government for the proceeds of insurance payable to named beneficiaries other than the insured's estate, but, if the insured has paid the premiums, any excess over the $40,000 exemption must be included in the gross estate. No Federal estate tax is levied on the proceeds of policies if the insured has not contributed either directly or indirectly to the payment of the premiums, provided, that at his death the proceeds are not paid to his estate.

Merely to mention the various State tax rulings which might have a bearing on business life insurance plans would require a fair-sized volume. Each life underwriter should make every effort to obtain accurate information as to the tax rulings in force in his own State and should refer doubtful questions to the proper authorities or to tax experts. The more effort a life underwriter makes to keep informed on general tax questions, the better equipped he is to obtain assistance from the right source when the need for specific information arises.

Those are the nine definite steps which can be taken to provide correct protection for a business need. Every need will necessitate a consideration of at least six steps—amount of protection—policy form—premium payment—beneficiaries—cash values—taxation. The other steps will be taken in such cases as demand their use. In addition, it is necessary to give some thought to the question of dividends or surplus distribution as they are made by participating companies, so the following paragraph explains the use of dividends in all types of business life insurance cases.

Dividends

Any discussion of the relative merits of participating or non-participating life insurance has been intentionally omitted. However, if participating life insurance is used some consideration should be given to the dividend distribution. A business organization is interested in net cost and for that reason the dividends should be applied to reduce the premium. However, an occasional variation of this practice is possible. If the insured, during the life of the policy, is rendered uninsurable the premium payer should immediately instruct the life insurance underwriter to apply

those dividends for the purchase of paid-up insurance. This additional protection will help to offset the discrepancy which will exist if other policies in the life insurance plan are increased at a later date. The dividends are the property of the premium payer irrespective of the beneficiary nomination except when an absolute assignment is in force. Some companies use an absolute assignment form in which the dividends are reserved to the premium payer. Others make the dividends the property of the assignee, and some make no reference to the subject. Such, in substance, is the summary of all points to be considered in regard to dividends and no mention has been made of their use in the later chapters. The status of dividends in relation to income tax returns has already been explained under the general paragraph on "Taxation" just preceding.

CORPORATIONS

CHAPTER III

CORPORATIONS AND LIFE INSURANCE

"A corporation is an artificial person created or authorized by the law for some particular purpose or purposes. It has, therefore, only those rights and powers which are given it by the law. . . . A corporation is usually composed of a number of persons associated together, though it may, and sometimes does, consist of but one or two members. These members, or stockholders, are not, however, the corporation. They compose it, but the corporation has a name, an entity, and an existence of its own, entirely apart and distinct from that of these members. Under its corporation name it may conduct business, make contracts, and bring suit. So absolutely different is the corporation's existence from that of its stockholders that it may enter into contracts with these latter, may sue them, or be sued by them." [1]

This comprehensive definition will perhaps serve to establish a clear conception of what a corpora-

[1] *Business Law,* by Conyngton, p. 377, Vol. 1.

tion is. In substance, those individuals who compose the corporation, by virtue of stock ownership, are obligated to join their interests with those of the corporation itself and to serve both with equal fidelity. The establishment of any policy of operation on behalf of, and by the executives of, a corporation must show sufficient justification to come within the interpretation of the following opinion:—"If an act is one which is lawful in itself and not otherwise prohibited, and is done for the purpose of serving corporate ends and is reasonably tributary to the promotion of these ends in a substantial, and not in a remote or fanciful sense, it may fairly be considered within its charter powers." (Steinway v. Steinway, 404 N. Y. Supp. 718). It has been generally held that the execution of some plan of life insurance on behalf of the corporation would be well within the meaning of this opinion just so long as the best interests of the corporation were being served.

Several court decisions have been handed down establishing the right of a corporation to carry life insurance under rather unusual circumstances. Exceptional as these cases were they have been upheld as valid. This would seem to substantiate the conclusion that, in general, the courts are aware of the splendid service which life insurance may

render to a corporation, and that, barring actual violations of the law, the life insurance plan will succeed. Whether it be a contest over life insurance policies or a disputed commercial practice of the corporation the courts today are very quick to protect a minority interest against invasion of its rights by majority stockholders. This protective attitude will do much to discourage wild life insurance plans which have been recommended, and in some cases put into force, with a minority interest totally disregarded. Bearing this thought in mind two suggestions are offered. First, a life insurance plan of any kind which is offered to one stockholder must be offered to all stockholders on the same basis. That is to say, a corporation cannot offer to buy the stock of one stockholder on a stated basis at his death with life insurance proceeds unless the same proposition is, at least, offered to all stockholders. Second, check this statement just made against the opinion of the corporation's attorney who is familiar with the law of the State in which the corporation is chartered. However, upon legal investigation it will undoubtedly be discovered that the substance of this opinion will hold good. The warning is sounded because there are many closely held corporations today which insist upon doing business as "incor-

porated partnerships." True, such corporations and their stockholders may sail on serenely and never be shipwrecked on the shoals of litigation. The life underwriter is only an experienced traveler with a discerning eye who may see trouble ahead and shout a warning. The lawyer, in the last analysis, must be the licensed pilot who will chart the proper course.

When a corporation enforces a business life insurance plan it is necessary for the board of directors of that corporation to record its vote of approval in the minutes of its meetings. The life insurance company which accepts the risk assumes that the application blanks have been signed by somebody duly authorized to perform that act. A business life insurance specialist makes it his duty to call the attention of his client to the necessity for this procedure. By the same token, if the corporation owns the policy and some time in the future wishes to surrender it to the insured for his personal possession, it can only do so by a recorded vote of the board of directors. Sufficient reason for the discontinuance of the corporation's insurable interest must be shown and it must receive a satisfactory consideration from the recipient of the policy in return. If the policy has been issued on a corporation form or if the corporation

has been the absolute beneficiary the life insurance company which issued the policy will request a copy of that vote before it will release the policy. It is obvious that the foregoing is based on the assumption that the corporation owns the life insurance. These legal restrictions are not applicable if individuals who happen to be a part of a corporation elect to execute some life insurance plan among themselves without involving the corporation as an entity in any way whatsoever.

In the last analysis, an intelligent application of business life insurance for a corporation demands at least a fundamental conception of corporation law. The underwriter can obtain a working knowledge of the subject for his own guidance, but, as previously remarked, the real guidance of the client should be delegated to a corporation attorney.

The inevitable conflict between the rights of a corporation as an entity and the desires of those persons composing it, plays a very important part in determining the procedure to be followed in applying life insurance to the many needs of that corporation. It must be remembered for purposes of accuracy in understanding the points outlined in this chapter that private negotiations entered into by persons who may happen to be component

parts of a corporation are not to be confused with agreements that are entered into by the corporation as such for its own benefit. For instance, two men may agree between themselves to carry life insurance upon each other's life for the benefit of the other in order that stock may be transferred to the survivor in the event of the death of either of them. In this case the corporation has no control over the situation, inasmuch as it is not financially involved. However, that corporation would be materially involved and its rights violated if these men proceeded to execute the same plan but insisted that the corporation should pay the premiums. This is an example of discrimination against all stockholders not participating in the plan as well as being unallowable because of the virtual absence of insurable interest on the part of the corporation.

Throughout the following discussion of business life insurance for corporations attention will be paid to the legal rights of the corporation. This phase of business life insurance cannot be emphasized too strongly and cases now in existence may be subject to invalidation of their original purpose because the originators have overlooked some outstanding legal complication.

CHAPTER IV

CREDIT REINFORCEMENT

The first major use of life insurance for the direct or indirect benefit of a corporation is to provide credit reinforcement. The execution of any subsequent insurance plan may be rendered null and void if credit is not taken care of. Life insurance as credit reinforcement should not be confused with its application under the subsequent consideration entitled "Direct Compensation." True, the two needs are quite similar and many times a corporation may provide life insurance to meet a need of "direct compensation" only to discover "credit reinforcement" as the real need—or vice versa. But, in reality, each one is separate.

It might be clearer to say that the reinforcement of credit must necessarily be considered with the corporation and its officers as borrowers. The term of obligation may be short, long, or indefinite. Life insurance can be measured to meet that term.

Some human asset in every corporation justifies

greater credit than its tangible collateral. There is a human value and a property value to every corporation. These can be called assets or liabilities according to any just appraisal. But, they must be considered separately even though they *may* be considered jointly.

The credit officer of any bank watches for the ever-increasing opportunity to add that reinforcement to the position of his creditors which can be obtained by protection against its financial loss as the result of death—or destruction of a human asset.

Life insurance establishes its value as such a medium of reinforcement because, like fire insurance on property, it constitutes replacement of that capital which may be lost in the destruction of a vital human value.

Fire insurance is responsible for immediate restoration of financial stability after many a fire. Corporations are acute in sensing this act. This theory, as applied to life insurance and a corporation, is exactly the same but the practice is woefully weak. Many corporations totter and fall when death removes the backbone of their credit. Many times competent executives have peeked out of the corner of their eyes at this highly probable

situation. If they would look straight at it and stare for a while, life insurance would loom in the imagination of these executives as the same potent reinforcing agent for their credit at the time of death as does fire insurance at the time of a fire.

Life insurance may be used to advantage in reinforcing the credit of a corporation:—

1. By liquidating bank loans or other first liens which have been granted on the strength of official and/or personal endorsements.

2. By amortizing bond or preferred stock issues as well as protecting them against depreciation if they are supported by key individuals who could be insured.

(a) The corporation might elect to amortize these securities at the end of a given time, in which case endowment insurance could be used as a sinking fund against such a plan.

3. By providing insurance on the life of one or more men equivalent to one year's interest on the securities mentioned above. Such a provision would assist materially in relieving the minds of investors. More than that, such interest on the bonds is a fixed charge and must be paid unless waived by legal right of the corporation.

4. By paying for outstanding contracts for

merchandise or raw materials the sale or conversion of which depend upon executives who are insurable.

5. By guaranteeing a customer against loss if the corporation has undertaken the execution of a contract or an order which will depend upon the continued existence of one or two men.

6. By insuring the treasurer of any corporation so that a fund for general reinforcement, if and where needed, may be available at his death.

These are the most common needs for credit reinforcement in a corporation. There are others which will present themselves from time to time. They may be subdivisions of those listed or entirely different. In each of these cases it is understood that the insurance should be placed on the lives of those men whose endorsements have been used or whose continued existence is essential to the maintenance of proper credit standing.

No corporation can justifiably avoid the small premium payment which will provide life insurance for the stabilization of the corporation itself. It will also give protection to those who have invested their money because they have faith in the acumen of its officers.

AMOUNT OF PROTECTION

It is very easy to determine the amount of protection which will be necessary if the outstanding obligations are always the same. It is not so easy if a corporation must obligate itself to varying amounts at different times throughout each year. If the obligation is fixed the protection should be split up among the responsible officers in amounts whose total will equal the obligation itself. If the corporation borrows money or merchandise in varying amounts the protection should be placed on the responsible individuals in an amount equal to a fair average of all outstanding credits at any time during a four or five year period just preceding. Almost any wool business affords a good example of the latter condition. Upon investigation it is found that such a corporation has had credit as high as $100,000 and as low as $10,000. It is also discovered that during the past three years $75,000 has been borrowed for about sixty per cent of the time. Consequently, if two officers of the corporation appear on the notes for this obligation, either as officers or as individuals, those men should be insured for $40,000 each.

In general, it can be said that almost any corporation can readily determine its own average

credit demand, and it can also know what men are responsible for the privilege of that credit. Hence, it is but one step further to place life insurance on these men.

POLICY FORM

It is quite safe to say that each case of credit reinforcement by life insurance would fall into one of two major classifications, i. e. limited and unlimited forms of obligation.

The first group would include the cases where endowment policy proceeds would be used to amortize the obligation. This has been used effectively in conjunction with bond issues and other comparatively long-term credits. It would also include such cases as demanded the use of term, modified life, or ordinary life insurance against credits for a short period with an option for renewal. In other words, if the term of credit is limited and if amortization is desired, use endowment insurance. Use term insurance if it is necessary only to have protection during the period of obligation and not to exceed five years. Use ordinary life if the period of obligation is indefinite.

The second group includes those cases of spasmodic borrowing for an unknown time. Ordinary

life insurance should be used in practically every case. Term or modified life insurance may be considered if the initial premium payment is of more importance to the corporation than the net cost. It should not be forgotten that ordinary life insurance shows a lower net cost after the fourth or fifth year than term insurance.

Regardless of the type of insurance, the policy should be on a corporation form of contract, if the company writing the insurance issues that form.

PREMIUM PAYMENT

The corporation should pay the premiums as all benefits of the policy should accrue to the corporation, and by paying the premiums the corporation retains basic control of the policy.

BENEFICIARIES

The corporation form of contract makes the corporation the absolute beneficiary and this is quite as it should be. If there is occasion to have the policy proceeds paid directly to a creditor this can be provided for by an assignment. Suffice it to say that with or without assignment it is always much better to make the corporation the initial

or primary beneficiary, thus permitting it to retain such rights in the policy as may be possible or desired.

ASSIGNMENTS

If a creditor is entitled to a direct interest in a policy of credit reinforcement that interest may be protected by either a collateral assignment or an absolute assignment. The former gives the creditor protection in the event of death to such extent as "his interests may appear." Furthermore, the creditor is at all times protected to the extent of his interest in the assets (cash values) of the policy.

The absolute assignment conveys all rights and title in the policy to the assignee to be retained till such time as the assignor shall discharge all obligations and thereby obtain a release of the assignment from the assignee.

These methods of protecting the interests of a creditor are most equitable and efficient. It is recommended that the proper form of assignment be applied in every case of credit reinforcement.

AGREEMENTS

There is seldom any need for a written agreement when protection is applied against credit ob-

ligation. To use such an agreement would mean that all terms of the contract between the insured and the beneficiary could not be expressed under the beneficiary clause of the policy, or under whatever form of assignment might be used. However, since no life insurance company can govern the disposition of funds once they have been paid to the beneficiary, an agreement might be necessary where some special disposition would be desirable. If this condition were to be present it would be necessary to consult an attorney and ascertain from him the information to be incorporated into a written agreement.

CASH VALUES

By referring to the paragraph entitled "Assignments" it will be noticed that cash values are considered as assets belonging to the assignee insofar as his interests may appear in a collateral assignment, and they belong entirely to the assignee if an absolute assignment is in force. Of course, this will naturally prevent the insured and the interests which he represents from obtaining any part of the cash values prior to the liquidation of their obligation to the creditor except with the consent of the latter. If, on the other hand, there are no restrictions on the policy, the cash value

is naturally a liquid asset of the corporation which is carrying the insurance. It may be declared or not in the balance sheet of that corporation as an "asset."

TAXATION

The rulings of the Federal income tax authorities do not permit the deduction of life insurance premiums on policies carried for credit reinforcement since the corporation would benefit directly or indirectly from the insurance in the event of the death of the insured. Under the Federal income tax law, however, the proceeds of policies paid at the death of the insured are not subject to Federal income tax, except in case of a transfer for a valuable consideration. But, if a corporation carries an endowment policy for the amortization of an obligation such as a bond issue, which matures during the lifetime of the insured, it will be taxed on the income which is represented by the difference between the net amount paid by it to the life insurance company in premiums and the amount it receives under the policy, if and when that difference is in favor of the beneficiary.

Each life insurance underwriter should acquaint himself with the details of his local inheritance or estate tax law in order that he may amplify

the following opinion when necessary. In general, it is safe to say that insurance carried by a corporation upon the lives of responsible officers for credit reinforcement is not subject to inheritance or estate taxes at the death of the insured, except as it can be definitely proved that the estate of the insured has been enhanced by the policy payable at his death.

Examples

A corporation found it necessary or desirable to increase its capitalization by a first mortgage gold bond issue of $1,000,000; $100,000 to mature serially each year on January 1, starting ten years from the date of issue. A life underwriter presented a plan to that corporation whereby its president should be insured under ten policies of endowment insurance of $100,000 each, to mature simultaneously on the date of retirement of each block of one hundred bonds. By this procedure the corporation provided a periodic sinking fund created by the payment of the life insurance premiums together with the complete protection against the loss of its president by death. Incidentally, this corporation could have varied this plan by splitting the insurance in equal amounts or variable amounts upon the lives of all four of-

ficers who were known to be primarily responsible for the welfare of the corporation.

A second example may be cited of a case quite similar to the one just outlined. The corporation in question needed immediate financing to the extent of $100,000. Its credit at the bank was good for that amount provided the notes were endorsed by responsible officers. It was also requested that those notes should be accompanied by a certain amount of collateral, which was $25,000. Now, in this case, the bank demanded $100,000 ordinary life insurance upon two officers, the senior vice-president and the treasurer, in amounts of $50,000 on each man.

CHAPTER V

DIRECT COMPENSATION

The Valued Employee or the Expert

Almost every corporation has in its employ some man or men whose particular adaptability to execute their work constitutes an asset in terms of money to that corporation. The man may have general ability which is applied along specific lines. One of the most concrete examples of this type is the sales manager who is quite familiar with many phases of the corporation's business, but whose particular training is concentrated upon the sales problem. It should be remarked that there is a distinction to be made here between the sales manager who is an employee, and the sales manager who is a stockholding executive in the corporation. The sales manager may be entrusted with the execution of a sales program to such an extent that his loss by death would mean the loss of money to the corporation.

On the other hand, there is the expert who is

capable only of doing one particular thing, but whose highly developed knowledge makes it very difficult to replace him except at great expense. He has developed methods or formulas which are essential to the welfare of the corporation's business, and for that reason he represents an actual cash asset to the corporation.

The subsequent paragraphs give consideration to providing proper protection to the corporation in the event of the death of either the valued employee or the valued expert. The method of meeting the need for protection is the same in either case.

AMOUNT OF PROTECTION

In such an instance the amount of protection can be determined by a single formula or by a combination of formulas. Take an amount equivalent to ten years' salary for the man; or an amount equivalent to contracts, whose execution depends upon this man; or an amount which would provide a large enough purchase price to obtain his successor in the open market. In this connection it should be remembered that any man competent to replace a lost expert is usually satisfactorily situated and a stock or cash bonus is

often necessary to lure him away from his present position. If the man in question happens to be an important cog in the sales machine, the amount of protection should be based upon the value of the business which he positively controls, as this business may be lost to the corporation in whole or in part if the man dies. Furthermore, there will be the added expense for training a new man and acquiring new business to replace that which is lost. This should be reckoned in determining the amount of protection.

POLICY FORM

Ordinary life is recommended as the best medium of protection, for it will provide the greatest amount of permanent protection and its net cost over a period of years will be less than that for term insurance. The corporation form of contract should always be used in cases of this kind if the company accepting the risk issues that special form.

PREMIUM PAYMENT

It will be shown subsequently that the corporation is to be the beneficiary under these policies,

and in view of that fact it is expected to pay all premiums.

BENEFICIARIES

When the corporation form of policy is used the beneficiary is automatically invested with absolute rights under the contract. There can be no variation of this relation except by duly recorded vote of the board of directors, and upon the receipt of proper consideration for such action. When the policy matures at death, the proceeds go directly to the corporation treasury, and constitute a discretionary fund.

If the insurance company which is to accept the risk does not issue a special corporation form of policy, it is necessary that the nomination of the beneficiary shall be made to conform with all requirements of the insuring company. Inasmuch as these requirements vary widely it will be necessary to refer to the proper authorities in each case in order to determine how that nomination should be stated. Under no circumstances should the beneficiary clause be drawn in such a way that any of the proceeds of the policy could revert to the benefit of the person insured.

ASSIGNMENTS

In this type of case there is seldom any use for assignments, inasmuch as the contract is a direct compensation to the corporation with all right and title fully protected by the correct beneficiary clause.

CASH VALUES

As explained under "Beneficiaries" the rights of this policy are held by the corporation as the absolute beneficiary. This would mean that the increasing cash values of the policy constitute a quick asset, to be declared in the balance sheet or not, as the corporation may elect. It should be remembered that the cash values in any form of term contract are negligible.

TAXATION

The premiums cannot be deducted as an expense of the business in making Federal income tax returns because they represent premiums paid on a policy, the proceeds of which will go to the corporation at maturity.

No inheritance tax or estate tax would be levied on the proceeds of a policy of this type at

the death of the insured, for he would not contribute directly or indirectly to the payment of the premiums and the proceeds, as such, would not become a portion of the insured's estate.

Examples

A corporation had established a very successful business in the manufacture of shoe laces. They were very much in advance of their competitors because of the inventive genius of a man in their employ. He invented a machine which would attach a metal tip to a shoe lace in a much more efficient manner than had ever been done before. His inventive ability meant so much to that corporation that they insured his life for $250,000 according to the method outlined in the preceding paragraphs.

The private secretary to the manager of a shipping concern so thoroughly informed herself of her employer's business that she became virtual manager of certain aspects in the work. The corporation, being old and established and held closely by the family, could not provide her with stock participation. Of course, her salary was in proportion to the work which she did, for she had made herself invaluable to the organization. Her

employer now carries insurance on her life to cover the contingency of loss in the event of her death.

Contracted Parties

There is very little difference between the need just outlined and this discussion of the insurable interest which a corporation may have in an individual or group of individuals not in the direct employ of the corporation, but rather under contract to it, for the execution of certain work.

The chief difference, however, lies in the fact that the contracted party is only responsible for the execution of one particular piece of work for the corporation, and the services of this party are not necessarily wholly at the disposal of the corporation. The insurable interest lies in the fact that the successful completion of the work depends upon the ability of one or more men whose lives can be insured. This is a very frequent consideration for business life insurance, and is consequently discussed as a separate subject. Special attention should be paid to the use of assignments in providing the proper protection of the rights of all parties concerned.

AMOUNT OF PROTECTION

The amount of protection should be based upon the part played by each individual in the execution of the contract. If special knowledge is imparted, the loss of which would jeopardize the completion of the work, life insurance should be carried for at least fifty per cent of the contract, and preferably for the full amount. If the passage of time plays any part in the diminution of hazard, it is well to strike an average of the risk involved as this will in part remove the possibility of a speculative feature in the use of life insurance. The corporation should be able to estimate to a very fine degree just how much money would be involved at any particular point during the execution of the contract, and the amount of protection will necessarily be governed by this computation.

POLICY FORM

Usually the most satisfactory form of insurance to use would be ordinary life. Its advantages are embodied in its low net cost over a period of years and its flexibility from the point of view of the beneficiary as well as from the point of view

of the insured if for any reason it became desirable to surrender the policy to the latter. If the insuring company issues a special corporation form of policy it should be used in this instance. It is obvious, if the contract has to run for a period of only one or two years, that term or modified life insurance would be the most desirable form to use.

PREMIUM PAYMENT

The premiums should be paid by the corporation unless there is some stipulation in the contract that the contracted party shall carry the insurance himself. However, in any case, it is more desirable for the corporation to carry the insurance since it then retains full control and derives full benefit.

BENEFICIARIES

It is understood that in all cases of this kind, the corporation should be the beneficiary if it is paying the premiums. This provision should be protected by using a standard corporation form of policy, or a corporation beneficiary clause as prescribed by various companies. The nomination should be made so that the contracted party

could have no access to any of the benefits under the policy. If the contracted party is paying for the insurance the policy should be made out with the insured's estate as the beneficiary, provided, of course, that the insured and the contracted party are one and the same. If, on the other hand, the insured is merely a representative of the contracted party, the policy should be made out with the contracted party's company name appearing as the beneficiary. In each of the instances just cited these beneficiary nominations should be immediately supplemented by a collateral assignment in behalf of the corporation to which the contracted party is responsible.

ASSIGNMENTS

If the corporation is paying the premiums on the life insurance no assignment is necessary on new insurance. However, there is the possibility that the contracted party might already be carrying protection of his own which he would wish to have available for the corporation. In this case he could execute a collateral assignment on behalf of the corporation after having first adjusted his policies so that his estate would appear as his beneficiary. The corporation would then pay the

premiums on the policy and at the same time have their financial rights protected insofar as their interests might appear. If the contracted party is paying the premiums the standard form of policy contract should be used, and the insured must execute a collateral assignment of his interests to the corporation, thus making it possible for the latter to obtain full benefits from the protection.

CASH VALUES

When the corporation form of policy contract is used the cash values are a corporation asset without rights to the insured.

It should be understood if a collateral assignment is in effect that the rights to the cash values are vested in the assignee and cannot be considered in any way as assets of the insured.

TAXATION

Premiums so paid by the corporation are *not* deductible as an expense in making Federal income tax returns. If the insured pays the premiums, the Federal tax authorities might possibly allow the deduction provided no benefit would accrue to the insured, directly or indirectly through the payment of the proceeds at his death. There is no

specific ruling covering this point, however, and, the deduction should be made only on the advice of the lawyer for the insured.

If the corporation has actually paid the premiums on the insurance no inheritance or estate taxes would be levied against the life insurance proceeds when paid to the corporation. On the other hand, if the insurance has been carried by the contracted party, that is, if the insured has been the premium payer, it is possible that the proceeds of the policies might be regarded by Federal and State tax authorities in the same light as any other personal insurance. In this event, if the policy were payable to the corporation at the insured's death, the policy would be entitled to its share of the $40,000 exemption allowed under the Federal estate tax law, but any excess would have to be included in the insured's gross estate.

Examples

An expert on special equipment was contracted with to design and construct a plant with machinery for a big woolen manufacturing corporation. He was to supervise the work because his training and ability made his services essential to the success of the project. At the time the corporation

entered into negotiations with the contractor it knew that on November first it would be forced to vacate its factory which had been sold out from under it, and which, as a matter of fact, had ceased to be adequate for the work. Unfortunately the time element was a very important factor and the agreement with the contractor specified a bonus of $25,000 if the contract, which was to be executed on a cost plus basis, was completed by November first. The corporation relied upon the known ability of the contractor to perform this task, and since a delay or misfortune, which might be caused by his death, meant a severe handicap to the operations the corporation immediately insured his life for $150,000 on a one year renewable term policy.

Here is another interesting example of this form of protection. A corporation, engaged in the manufacture of steam fittings, had suffered severe losses as the result of poor management and an equally poor market. However, the business was old and had been well established. Its name was well regarded, and there was no reason why it should be allowed to slip into the discard without a struggle. The board of directors of this corporation had the commonsense to turn for assistance to a professional industrial manager who

contracted to re-establish the business on a paying basis within seven years, with the added proviso that he was free to retire or remain, as best suited his interests, at the expiration of the seven year period. Since the directors of the corporation had thus placed "all their eggs in one basket" their judgment prompted them to obtain as much protection for that "basket" as they could afford. An ordinary life policy of $200,000 was taken out by the corporation on the life of this temporary president. This form was used because, although the contract period was for an initial term of seven years, they had no way of knowing how long they might retain an insurable interest in this man's life.

Officers of the Corporation

Direct compensation for the loss by death of the human asset invested in the lives of corporation officers is a very important phase of business life insurance. It differs from insurance on employees because the officer or his estate—assuming him to be a stockholder—will obtain some share of the benefit. It may readily be seen that the value of the stock which the officer holds must be enhanced if the corporation has provided cash

compensation by life insurance for loss of his life value.

Furthermore, from the point of view of the corporation itself such protection is essential. Many times an officer is invested with powers which give him great latitude. He may be undertaking projects or policies in behalf of the corporation which demand his personal supervision. If he should die during the developments, the corporation would lose money. This vital interest is insurable. Most officers constantly strive to make themselves indispensable. Most corporations unconsciously encourage this ambition. Yet many corporations fail to back it up with life insurance, and as a result they find themselves embarrassed if such a valuable officer is suddenly withdrawn by death. Right here it seems wise to make the point that all deaths *in business* are sudden.

If a man is stricken ill and death follows at the end of a protracted period of inactivity such a loss will have been anticipated. A successor will be on the job and ready to take up the duties of the sick man if he should die. Hence, the man is not in the business at death. This is all by way of saying that if a man dies while he is "in the harness" his death is sudden and without warning.

In any case, life insurance provides what is often called a "shock absorber." Quick and unencumbered capital is very welcome when adjustment is necessitated by the death of any officer.

AMOUNT OF PROTECTION

It is reasonable to take protection equivalent to five or ten years' salary plus a proportionate share of the good will. Again, if there are outstanding obligations in the name of the officer but in behalf of the corporation the protection should equal the amount of those obligations.

In the case of protection against the general value of an officer this formula may be used. Take a figure to include invested capital and quick assets and subtract a six per cent yield on this principal from the gross income actually earned. The result is an estimate of the worth of the human assets in that business. Then apportion to the officer or officers the proper share of responsibility for that profit and insure accordingly. For example, a corporation has two officers who are solely responsible for a gross profit of $30,000 on an investment of $100,000. A six per cent return is more than fair for $100,000 invested in securities. Thus the balance of income or $24,000

represents the earning capacity of the brain power. Each man is worth $12,000 a year, or about $60,000 of life insurance on each life.

POLICY FORM

Ordinary life is almost universally used in a case of this kind, and the policy should be on the corporation form. There are times when the necessity for low overhead demands term or modified life insurance, but the permanency of the protection recommends the use of ordinary life. There is occasional interest in the limited payment life policies. They should only be used when a corporation has a definite reason for cleaning up the premium payments as soon as possible. This is an instance when a limited payment life policy might be used because the cash values of such a form would be higher and consequently more desirable.

PREMIUM PAYMENT

The corporation gets the proceeds, therefore it pays the premiums. There should not be any deviation from this method unless, of course, the policy is released to the insured in which case the corporation ceases to be the premium payer.

BENEFICIARIES

The corporation is made the sole beneficiary under the corporation form of policy contract, and it should be properly named in all the standard policies not known as corporation form. The corporation *must* be the direct beneficiary if it pays the premiums. There is a possible exception to this rule, and that is the case where a corporation pays the premiums on policies in favor of the insured's beneficiaries but with the purpose of being the ultimate or indirect beneficiary of the plan. However, close scrutiny of this plan will reveal the fact that the insurance is a gift to the insured in return for valuable services. This being the case the plan seems to come within the classification of personal life insurance rather than business life insurance. No other deviation should be made from this procedure without consulting a lawyer and a business life insurance expert.

AGREEMENTS

In some cases of this kind it may be desirable to execute a written understanding as to the exact disbursement of the life insurance proceeds. The officers of a corporation may agree among them-

selves that such proceeds shall apply against certain obligations in order of importance and insofar as the proceeds will last. This should be expressed and subscribed to by the corporation in writing, and the document should be prepared by the corporation's attorney.

CASH VALUES

The cash values in this case are a quick asset of the corporation, and may be declared or not at the discretion of the corporation. They may be borrowed in time of grave need and applied for general use by the corporation.

TAXATION

The corporation cannot deduct the premiums as expense in making Federal income tax returns, but as in the previous cases, the proceeds of the policy paid at the death of the insured need not be declared as income in making Federal income tax returns except in cases where there has been a transfer for a valuable consideration.

If the corporation has paid all the premiums on a policy which is paid to the corporation at the insured officer's death, the proceeds of the policy, as such, would not be subject to estate or in-

heritance taxes. If the insured officer is a stockholder, however, the value of his holdings may reflect this increase in the assets of the corporation when appraised for Federal estate tax purposes, for the Federal tax authorities hold that the proceeds of a policy payable to a corporation at the death of the insured increase the assets to the amount of the face value of the policy. State rulings differ on the question of whether the corporation's assets are increased by the cash value or the face value of a policy paid at the death of the insured. The Court of Appeals of New York, in a recent decision, took the same view as does the Federal Government; namely, that the corporation's assets are increased by the face value of the policy. The question is of particular importance from a tax standpoint only in cases where the insured officer owns a relatively large amount of stock in the corporation and the value of his holdings might be considerably increased by the increase in the corporation's assets.

Example

Two men had originally organized a partnership, which was later incorporated, to engage in the razing of buildings. Even as a corporation

they were very early in the field of this highly specialized form of work. Ultimately one of the men became incidental to the success of the corporation, and the other man became very instrumental in building it to its comprehensive proportions. When he was at the height of his productivity that corporation took out policies aggregating $150,000 of ordinary life insurance on his life, payable direct to the corporation. Competition in the field became keen, and as a result of overwork and other harassing conditions in the business he became demented to such a point that he could not stand the strain and died. After the affairs of the corporation had been adjusted it was discovered, and this statement was issued by the corporation, that this life insurance had made it possible for it to remain in existence on a solvent basis, whereas without the insurance it would have been bankrupt at the time of its president's death.

CHAPTER VI

LIQUIDATION FUND

Stock Purchase Plan

This is one of the most efficient applications of life insurance to a business need. It is especially interesting to all corporations which are closely held and which wish to remain so even though one of those stockholders should die.

There are many corporations which are virtually partnerships or proprietorships except for the limitations defined by their corporation charters. The success of the business has been based solely on the ability and acumen of one, two, or three men. These men may feel that they wish to have their estates or their beneficiaries free from business worry and for that reason want their stock bought by the corporation. Or, they may feel that the corporation should always be owned by the surviving members of the originating group.

Consequently, the men may say one to another,

"I want to be free to pursue my own policies after you're gone, and I presume that you are of like mind. Therefore, I want to be able to buy up your stock so that there will be no chance of that stock falling into unfriendly or inexperienced hands." Thus the owners of the closed corporation covenant one with another that their stock shall be bought in for a "fair" price by the survivors or by the corporation at the times of their deaths unless there is some statute which prohibits the corporation from purchasing its own stock. This fair price can be determined by an appraisal previously arranged and the understanding should be definitely drawn up in writing.

Life insurance plays its part in this way. It provides this purchase price or known amount immediately upon demand at that unknown time when death will occur. The corporation or the individuals themselves take out policies of insurance on the lives of those men who wish to participate. Thus, the funds are provided with which to purchase the stock of the deceased associate.

If life insurance were not used, long term obligations to the estate might be necessary and these would provide a fair share of additional worry for the survivors. Furthermore, if the business of the corporation is subject to seasonal

fluctuations or to other "peaks" and "valleys" throughout the year, a death might occur when it would be very awkward for the corporation or the individuals to take working capital or bank credit for the purchase of this stock interest.

AMOUNT OF PROTECTION

It is quite easy to determine the proper amount of protection. The accurate way is to make an appraisal of the value of the stock held by each participant in the plan as of today. The insurance on the life of each man is an amount equivalent to the value of his stock.

Right here it should be remarked that the amount of insurance should be increased over this formula in the case of any man of advanced years, or in the case of any man who is not a standard physical risk. This is recommended because the insurance in force should always equal the advancing value of the stock, and in the two cases just mentioned, it might be impossible to avoid a grave discrepancy in later years between the value of the stock and the insurance carried. In other words, the interested parties should place all the insurance possible *now* on those lives where the

future insurability may be menaced, or where the subsequent premium may be prohibitive.

On the standard risks, as stated before, the amount of protection should equal the value of the insured's stock with the anticipation of increasing the amount in proportion to the increasing value of the stock from year to year. Of course, there is no guarantee that this risk will continue to be standard so it is prudent to place just as much life insurance as possible. This will be anticipating an appreciation in the value of the stock as well as securing all the insurance possible while the risk is known to be standard.

POLICY FORM

Again we turn to the standard medium of business protection—ordinary life. Limited payment forms of ordinary life may also be used where all concerned are ambitious to have the policies paid up. However, limited payment forms should not be used on the older ages. Endowment forms are used occasionally when the contracting parties to a stock purchase plan wish to have their interest bought out during their lifetimes. Thus, if a stockholder wished to retire in twenty years a twenty year endowment policy would provide the funds

with which to execute the stock retirement at the expiration of that period or before, if he died.

PREMIUM PAYMENT

An explanation of premium payment in a stock purchase plan must be made simultaneously with the discussion of beneficiaries, so the two subjects will be considered jointly in the following paragraph.

BENEFICIARIES

It must be remembered at this juncture that a corporation has rights which are protected by law. These rights cannot be suddenly ignored by any plan which includes the corporation in name but not in fact. This statement is made because many unintentional violations of corporation law by all parties to a life insurance plan for stock purchase have been discovered.

So, if the corporation pays the premiums on a policy under this plan it should be the direct or indirect beneficiary. The parties to such a plan should not make the insurance payable to each other or to their estates and then pay the premiums with a corporation check, unless exceptional circumstances warrant contrary action

which should be endorsed by the corporation's attorney. If the corporation is to be the beneficiary under the policies the proceeds are paid into the corporation treasury, and such stock as is purchased by these funds can be resold or retired as treasury stock or declared as a stock dividend.

However, these funds can be reached by creditors of the corporation, and in this way the execution of the stock purchase plan may be impaired.

True, the corporation as beneficiary is not the ideal arrangement. It is infinitely better for all parties concerned to make the insurance payable one to the other or each to the others as the case may be. In this way many complications are avoided, and the contract can be promptly and efficiently executed. In the party-to-party plan, premium payment must be made from personal funds created by equal contribution from each man or by any other sharing of contribution which is equitable and fair to all concerned. However, in this case it is essential that the beneficiary shall have all rights to the policy under an absolute assignment.

As has been pointed out in the general consideration of beneficiaries on page 31, it is seldom wise to name wives as beneficiaries under a stock purchase plan unless they have actually participated

in the management of the business. Many times there may be legal complications arising from the actual ownership of the stock, and underwriters should not overlook the fact that a widow cannot give stock which she does not own. The possibility of disappointment over the size of settlement as contrasted with the income which the insured has provided, frequently makes the widow a cause of embarrassment to the survivor or survivors if negotiations are conducted directly with her. For these reasons, many stock purchase plans are being executed today in favor of a trustee, thus making the post-mortem transactions as impersonal as possible. Where this form of execution is elected the policies should be made payable to the trustee, and the premium payment may be made in any way desired except by corporation check. This trusteeship plan will be referred to in more detail in the paragraph on "Trusts."

ASSIGNMENTS

If the corporation has control of this insurance it is unnecessary to use assignments in any form, unless for some reason the insured has occasion to use old and outstanding insurance in order to comply with his part of the agreement. In this case he should, of course, execute a collateral as-

signment to the corporation so that it might have the benefits of its subsequent premium payments fully protected. If, however, the purchase of stock is arranged for on a party-to-party plan it is far more efficient and more binding if each party will take insurance payable to his estate, and then execute an absolute assignment in behalf of the other party. This may necessitate some adjustment in the agreement which will accompany this plan insofar as the cash values are concerned, but by and large it is safe to say that it is far better than making out the insurance direct to the beneficiaries without the use of assignments. Particular attention should be called to the fact that, during the execution of this plan and especially if assignments are being used, the corporation and the life insurance underwriter should ask for the competent assistance which can be rendered by the attorney for the corporation as well as by the legal department of the insurance company which has accepted the risk.

AGREEMENTS

The most important part of a life insurance plan for stock purchase is the written agreement which outlines and defines the execution of the plan. Such an agreement is one form of a "business

will" and it should be drawn up by the attorney for the corporation with such help as the life insurance underwriter and his company may be able to render.

All agreements should embody such salient points as the method of determining stock value at the time of the first death, the execution of the life insurance policies, the creation of the trust if there is to be one, the "minimum price clause," the disposition of the proceeds to the individuals, trustee, or corporation as the case may be, the transfer of the stock, the disposition of the insurance outstanding on the lives of the survivors including cash values at the time of the first death, a termination clause, and finally, the legal preambles, considerations, and conclusions.

It might be well to explain the "minimum price clause." It is current practice for all parties to agree that the estate of the deceased will not receive less than the policy proceeds as payment for his stock interest. This is a fair proceeding and it guarantees to each man a minimum sum which he knows his estate will receive for his shares of stock.

Attention is especially called to the agreement which is example 3 on page 105. This agreement affords a splendid instance of the ultra-modern

trend of the efficient combination of life insurance and a supplementary agreement. In the first place by reading paragraph 2 it will be seen that definite value is placed upon the shares of stock to be sold. The legality of this "set-price" feature has been generally substantiated because an owner of stock is quite at liberty to set a definite price on his stock. All of this is irrespective of a rise or decline in the market value of the stock. In New York State the courts have already refused to set aside an agreement of this kind (Scruggs *vs.* Cotterill *et al.* 73 NYS 882). Attention is also called to paragraph 4 in example 3. Here is a clause which might be considered foreign to a life insurance agreement yet it is a most practical insertion. From one point of view sub-paragraph (b) under paragraph 3 is the most important clause in the entire agreement. It might be called an "automatic declaration of a stock dividend." Without this clause but under this general type of agreement the stock purchased would be retired to the treasury of the corporation. This would mean that to remove the stock from that status a regularly voted stock dividend distribution would be necessary. With this clause added it may be seen that the stock dividend is automatically declared. This agreement is to be executed by a trustee, but it has

been included here because of its distinctive feature as an agreement.

It is impossible to outline every type of agreement which might be used. Each document should be the expression of the will of those who are a party to it, and each document should be drawn by an attorney at law. The best way to grasp the idea of a "business will" is to read the examples cited below.

Example 1

> In consideration of the mutual promises herein made, it is hereby agreed by and between the Doe, Roe & Co. Inc., a corporation existing under the laws of the State of New York, and John Doe, of New York in said State, for himself, and his executors or administrators, that on his death, but only in the event that Richard Roe, of said New York who, with the said John Doe, has been instrumental in building up the business of the said Doe, Roe & Co. Inc., shall survive the said John Doe for a period of at least thirty (30) days after his death, the executors or administrators of the said John Doe shall, not later than sixty (60) days after their qualification as executors or administra-

tors, sell, assign and transfer to the said Doe, Roe & Co. Inc., all the shareholdings of the said John Doe, in the said Doe, Roe & Co. Inc. at a price then agreed upon; or, if no agreement can be reached, at a price to be fixed by two or more of three appraisers, one chosen by the Doe, Roe & Co. Inc., one by the executors or administrators aforesaid, and the third selected by the two already appointed; provided, that if the shareholdings of the said John Doe are at least —— in number, the price to be paid therefor shall not be less than the sum of $——— as now fixed, but may be as much more as shall be agreed upon and fixed by the appraisers; and in the event that the value of the —— shares shall be found to be more than $———, then the sale and transfer of the shares shall be made pro rata at the appraised price. And the Doe, Roe & Co. Inc. shall accept any pay for the aforesaid shared in the manner and at the price fixed as herein provided, forthwith upon the tender made thereof in accordance with the terms of this agreement by the executors or administrators of the said John Doe, but it shall not be required to purchase and accept the transfer of

more shares than may be bought for $——— unless it so elects to do so.

Inasmuch as this agreement contemplates the sale and transfer of substantially all the shares now held by the said John Doe in the event that his executors or administrators shall be unable to transfer at least —— such shares, the Doe, Roe & Co. Inc. shall be under no obligations to purchase any of such shares unless it so elects to do.

It is further agreed that the Doe, Roe & Co. Inc. shall be entitled at any time on its option to demand and receive a bond of corporate suretyship, conditioned in the penal sum of $——— for the faithful performance by the executors or adminstrators of the said John Doe of his undertakings entered into by this agreement.

If the said John Doe shall be unwilling or unable to furnish a bond as aforesaid the said Doe, Roe & Co. Inc. shall, if it so elects, be released from its obligations under this agreement upon thirty (30) days notice in writing of its election to the said John Doe.

In witness whereof the Doe, Roe & Co. Inc. has caused this argeement to be signed in its name by its President and its Treasure

and its corporate esal to be hereunto affixed and John Doe has hereunto set his hand the —— day of ———— A. D. 1927.

Doe, Roe & Co. Inc.

(Corporate Seal)

By ————————
President

By ————————
Treasurer

(signed) John Doe

Example 2

WHEREAS, John Doe and Richard Roe, both of New York, King's County, New York, are the owners of the controlling shares of stock in Doe, Roe & Co. Inc., a corporation duly established under the laws of the State of New York, and having a usual place of business in said New York; and

WHEREAS, the parties hereto are mutually desirous of protecting each other in the continuance of the business and the interest and the ownership of the said controlling shares

of the survivor of either of the parties thereto; and

WHEREAS, each of the parties hereto is desirous that upon the death of the other the survivor shall become the sole owner of the controlling shares of stock in the said corporation; and

WHEREAS, the parties hereto mutually desire to protect their respective families by an offset to said shares of stock, which shall under this agreement go to the survivor of the other, and to provide therefor, have taken out the following policies of life insurance in the Ajax Mutual Life Insurance Company, to wit:

By John Doe, No. 23456 in the sum of Fifteen thousand ($15,000) Dollars, and No. 23457 in the sum of Ten thousand ($10,000) Dollars, both payable by assignment to the said Richard Roe; and

By Richard Roe, No. 23460 in the sum of Fifteen thousand ($15,000) Dollars, and No. 23461 in the sum of Ten thousand ($10,000) Dollars, both payable by assignment to the said John Doe; and

WHEREAS, the parties hereto have regarded and intend to continue to regard each

and every premium upon the said policies as a joint and several account and liability, to be paid by them in equal amounts.

Now therefore, KNOW ALL MEN BY THESE PRESENTS, that the said John Doe and Richard Roe, for themselves, their executors and administrators, agree as follows:

1. That the premiums on the said policies, or any policies substituted therefor, shall be paid in equal amounts by the parties hereto and shall be regarded by the parties hereto as their joint and several liability;

2. That on the death of either of the parties hereto the shares of stock in said corporation owned by the deceased shall be appraised by three (3) appraisers appointed in manner following: one by the survivor of the parties hereto, one by the legal representatives of the decedent, and one by the two appraisers already selected;

3. The said appraisers shall appraise the stock of the decedent in the corporation and determine the value thereof, and if the value determined as aforesaid shall exceed the proceeds received or to be received by the survivor on the policies of life insurance made payable to him by assignment as hereinbe-

fore set forth upon the life of the decedent, then, so many of the said shares equal at the appraised value the proceeds of said policies, and in case the appraised value of all of the said shares shall be less than or equal to the said proceeds of said policies then the total of the said shares shall belong to and be assigned and transferred to the said survivor;

4. That the executors and administrators of the decedent will assign and transfer the said shares of stock to the survivor of the parties hereto within sixty (60) days after the qualification of the said executor or administrator, and upon the payment of the said survivors to the said legal representative of the decedent of the proceeds of the said policies so received by the survivor upon the life of the said decedent;

5. Any shares remaining in the hands of the legal representative of the decedent, after compliance with the foregoing, shall in the time hereinbefore set forth be paid for and assigned to the survivors of the parties herein at their appraisal value;

6. That upon the death of either, the legal representative of the decedent holding by assignment the right to receive payment of

the policies upon the death of the other shall reassign to him the said policies on his life on receipt from him of one-half (½) of the cash surrender values of the said policies.

IN WITNESS whereof the parties have hereto and to an instrument of like tenor set their hands and seals this —— day of ——, 1927.

(Signed) John Doe
Richard Roe

Example 3

This agreement entered into by and between John Doe, Richard Roe, and George Goe, all of New York, N. Y., hereinafter called "ASSOCIATES," party of the first part, and the Doe, Roe & Co. Inc., of New York, N. Y., a corporation incorporated under the laws of the State of New York, hereinafter called the "CORPORATION," party of the second part, WITNESSETH:—

WHEREAS the associates are the owners of the entire stock of the Corporation; AND WHEREAS each of the associates is desirous of a protective market for his stock at a fair price in the event of his death: AND WHEREAS they are all desirous of being

assured that in the event any one determines upon the sale of any of his stock during his lifetime the others will be given the opportunity to purchase the same at a fair price:

WHEREAS all the parties hereto are desirous of maintaining control of the corporation's stock in order to insure a continuity of policy and management of the business of the corporation in the event of the death of any of the associates, and to maintain the ownership of the stock in the hands of the persons who shall be actively engaged in the business of the corporation.

NOW THEREFORE in consideration of the mutual benefits to be gained hereby and of the covenants and agreements herein contained to be performed by the parties hereto; and in further consideration of the issuance of certain policies of insurance on the lives of the associates, which policies are specifically listed in the Schedule marked "A" attached hereto and made a part of this agreement, made payable to the corporation as TRUSTEE under the terms of this agreement, and the payment of the premiums thereon by the corporation, the associates agree with

each other and with the corporation, jointly and severally as follows:

1. That the said corporation hereby acknowledges receipt, as trustee, of the insurance policies listed in the Schedule hereto attached marked Schedule "A"; that further policies of insurance may from time to time be delivered to the said corporation as trustee by joint action of the parties hereto, or policies of insurance may be withdrawn by joint action of all the parties, the description of which (the policies added or withdrawn) shall be attached hereto in Schedules numbered consecutively; and that the premium on the said policies shall be paid out of the funds of the corporation by the corporation's treasurer.

2. That the associates hereto for the purpose of this agreement only, have mutually agreed upon the net worth of the stock of the said corporation and have listed against the name of each associate the net value of his shares of stock as of ———, 1927, which agreement has been entered upon the books of the corporation over the signatures of the associates; and that annually on the —— day of ——— of every year hereafter sim-

ilar agreements of the then net worth of the said stock of the said corporation shall be made, agreed upon and entered upon the books of the corporation, all of which said agreements shall for the purposes of this agreement only, be binding upon the associates and their respective executors, administrators, heirs and assigns. The failure of the parties hereto to enter into an agreement upon the —— day of ———— in any year shall not void this agreement, but each agreement executed as above provided, shall stand in full force and effect until a subsequent agreement has been made.

3. That upon the death of the first of the associates to die:—

(a) The stock of such deceased in the corporation shall be sold to the corporation as trustee, and as such the corporation shall purchase the said stock with the proceeds of the policies held hereunder on the life of the deceased associate at the valuation fixed by the agreement with relation thereto made last preceding his decease.

(b) The stock so purchased by the corporation as trustee shall be redistributed to the surviving associates, the same to be di-

vided among them in proportion to their then present holdings of stock in the corporation.

(c) The corporation as trustee shall exert its best efforts to collect and receive all sums payable under the policies on the life of such deceased associate, then held by it under this agreement.

(d) The executors or administrators of the said deceased associate shall surrender and deliver to the corporation as trustee all stock of the said deceased in the corporation and shall execute all proper instruments and do all things necessary to effect a legal and equitable transfer of the said stock of the deceased associate in the corporation to the corporation as trustee when required to do so by it.

(e) If the proceeds of the policies of insurance on the life of such deceased associate shall be less than the net worth of his stock in the said corporation as fixed by the agreement with relation thereto made last preceding his decease, the said surviving associates shall execute and deliver to the corporation as trustee an agreement to pay the difference to the executors or administrators of the said deceased associate in three equal

monthly payments beginning thirty days after the appointment of the executor or administrator of said first associate to die, without interest.

(f) Upon due performance of the provisions of the preceding sections (c), (d), and (e) of this paragraph 3 the said corporation shall pay the purchase price of the stock transferred to it, or if the insurance proceeds be less than the purchase price as herein determined, said trustee shall deliver to the executors or administrators of said deceased associate all the proceds of the policies upon the life of the deceased and any agreements and notes which the said surviving associates may have executed in accordance with section (e), and to the surviving associates the corporation as trustee shall deliver all the policies of insurance upon their respective lives which may then be in its possession under this agreement, upon payment to the corporation of the then cash surrender value by each recipient of his respective policies, unless such associates shall execute a new agreement with the corporation as trustee for the continuance of this trust and all the stock of the said deceased associate in the said corporation

shall be delivered to the said surviving associates in the proportions that their then present individual holdings bear to their joint holdings.

4. That if any time any associate desires to dispose of his shares of stock in the corporation or to offer the same for sale or any part thereof, such shares of stock shall first be offered for sale to the remaining associates at the price fixed by the agreement provided for under section 2 of this instrument, and the associates shall be given written notice of such intention and the parties so notified shall have two months from the date of the receipt of such notice within which to take advantage of the terms of this contract and in the event they or any of them fail to avail themselves of such terms, the associate wishing to sell shall be free to sell his stock to such person, for such price and upon such terms as he may elect and generally to make such disposition of the stock as he shall choose. The entire stock offered by the associate for sale under the terms hereof shall be divided among those remaining associates who elect to avail themselves of the privilege of purchase in the proportion that their then present hold-

ings bear to each other. This election to purchase is intended to give each associate or any of them the right to purchase the entire stock offered for sale or any portion of each associate's allotted number of shares in the stock offered for sale.

5. The corporation hereby covenants and agrees with the associates that it will pay the premiums due on the insurance policies listed in Schedule "A," or any subsequent Schedule, while this agreement is in force, and that upon the death of the first of the associates to die, it will make no claim against the proceeds of the policies of insurance upon the life of the deceased, or upon the policies upon the lives of the surviving associates, because of premiums paid by it, or for any other cause whatsoever, and it hereby expressly waives any lien or other rights which it may have now or at any time hereafter, or against the policies upon the lives of the associates or any of them, or the proceeds thereof.

6. That this agreement may be revoked or amended at any time by the mutual consent of the parties hereto.

7. That the corporation shall act as trustee without compensation.

8. This agreement shall be binding upon the associates, their heirs, executors, administrators and assigns, jointly and severally and the corporation, its successors and assigns.

IN WITNESS WHEREOF the parties hereto have signed their names and affixed their seals this —— day of ———, 1927.

(Signed) John Doe
Richard Roe
George Goe

It is always a good plan to refer contemplated agreements to the legal department of the company issuing the insurance. This accomplishes the twofold purpose of obtaining added advice from competent authorities as well as preventing the execution of any contract so affecting the life insurance that its usefulness might be destroyed. No insurance company, however, will assume responsibility for the validity of an agreement as it is not within its power to do so.

TRUSTS

The use of a trustee for the execution of a stock purchase agreement is quite frequent today. There are many advantages, not the least of which is in having an impersonal "third party" who has all

interests in equal proportion and who will act as a guiding factor in the satisfactory completion of the agreement. Consultation with the trust officer of any bank will prove the effectiveness of such coöperation.

Two specimen agreements are copied below, each embodying the use of a trustee to execute the provisions of the agreement. In addition to these trust agreements there is example 3 under "Agreements" just preceding. This is worthy of serious consideration by any trust officer or lawyer who has been retained to draw up such a plan.

Example 1

THIS AGREEMENT, made this —— day of ———, A. D. 1927, between John Doe, first party, Richard Roe, second party, and the Broadway Trust Company, third party, WITNESSETH:

WHEREAS, John Doe and Richard Roe are each owners of —— shares of the capital stock of Doe, Roe & Co. Inc., a New York corporation with an authorized capital stock of $——— consisting of —— shares of the par value of $——— per share, and

WHEREAS, it is the desire of first and second parties hereto, in consideration of ——— paying the premiums upon the life insurance policies hereinafter described, upon the life of each of the first and second parties hereto, said policies being payable to the Broadway Trust Company, Trustee, of New York City, third party, for the benefit of the wife of first party, and of the wife and daughter of second party, or either of them, that all of the above mentioned shares of stock of each of first and second parties hereto, together with all additional shares of stock in said company which either or both of them shall hereafter acquire, shall be purchased by the survivor of the first and second parties hereto upon the death of either of them who shall first depart this life, having a part or all, as hereinafter set forth, of the proceeds of said insurance policies upon the life of the then deceased party applied upon said purchase price, which shall be determined by the then book value of said stock.

Now, therefore, it is agreed as follows:

That, in consideration of the covenants herein contained and the payment to third

party of one dollar and other valuable considerations by each of the first and second parties, the receipt whereof is hereby acknowledged, and in further consideration of the issuance of certain life insurance policies herein mentioned and the payment of the premiums thereon by said Broadway Trust Company upon the life of said John Doe, and the life of Richard Roe, as follows:

Upon the life of John Doe:

Policy No. 98765, dated June 15, 1927, issued by the Ajax Mutual Life Insurance Company, providing for the payment upon accidental death of said John Doe, the insured of $———, and in case of death from other causes $———, and providing for disability benefits in case of sickness or of accident to the insured; and Policy No. 98790 issued by the Ajax Mutual Life Insurance Company, on July 10, 1927, for $———.

Upon the life of Richard Roe:

Policy No. 98766, dated June 15, 1927, issued by the Ajax Mutual Life Insurance Company, providing for the payment upon accidental death of said Richard Roe, the insured, of $———, and in case of death

from other causes $———, and providing for disability benefits in case of sickness or of accident to the insured; and Policy No. 98791 issued by the Ajax Mutual Life Insurance Company, on July 10, 1927, for $———.

That upon the death of either of first or second parties hereto, who shall first depart this life, all of the above mentioned shares of stock of Doe, Roe & Co. Inc., belonging to the then deceased party hereto shall be purchased by and assigned, sold and set over unto the surviving of said parties, at the then book value of said capital stock.

That the Broadway Trust Company, third party, to whom said policies are made payable, as Trustees, shall, upon the death of either of said parties who shall first depart this life, receive the proceeds of said policies then payable, and for that purpose shall have full power to collect the same and execute and deliver any receipt or voucher for the same.

Said third party, out of the proceeds of said Life Insurance policies, shall pay to the estate of the then deceased party, a sum equal to the par value or the book value, whichever

is greater, at the date of such decease, of all the capital stock in Doe, Roe & Co. Inc., belonging to the then deceased party and any amount remaining in the third party's hands out of said proceeds after the payment of the above mentioned sum to the estate of such deceased, shall be paid forthwith to ———, and in the event that the proceeds of said Life Insurance policies received by third party shall be insufficient to pay to the estate of the then deceased party a sum equal to the par value or the then book value, whichever is greater, of all of said capital stock belonging to said deceased party at the date of his death, then the survivor shall within one year from the date of death of such deceased party, pay to the latter's estate, without interest, a sum equal to the deficiency on the book or par value of said stock, whichever is greater, as above set forth.

Upon the death of either of the first or second parties hereto, who shall first depart this life, and the payment of the Life Insurance proceeds by the third party and the delivery of said capital stock, and the full pay-

ment of said book value of said stock, all as hereinabove set forth, this contract shall be fully terminated and ended, and third party shall forthwith deliver to the survivor of the individual parties hereto the above described insurance policies upon the life of the latter.

First and second parties hereto have delivered the above described policies to the third party, the receipt of which is hereby acknowledged, and said policies shall be retained by third party until the termination of this agreement as above set forth.

This agreement shall be binding upon the insured to the benefit of the heirs, executors and administrators of the first and second parties hereto, and may be altered or revoked at any time at the option of first and second parties hereto.

In witness whereof, first and second parties have hereunto set their hands and seals and third party has caused these presents to be signed in its corporate name by its President and its corporate seal hereto affixed, attested by its Cashier, the day and year first above written.

_____ (Seal)
First Party

_____ (Seal)
Second Party

Attest:

_____ _____
Cashier

By _____ President
Third Party

Example 2

This agreement, executed and delivered in the city of New York, N. Y., this thirtieth day of January, 1927, between John Doe and Richard Roe, both of said New York, parties of the first part, and the Broadway Trust Company, of New York, hereinafter called "the trustee," party of the second part, witnesseth:

That whereas the said John Doe and Richard Roe have each deposited with the said trustee certificates endorsed in blank for —— shares of stock in the Doe, Roe & Co. Inc., a corporation organized under the laws of the State of New York, and have also each nomi-

nated the said trustee as beneficiary under policies of insurance on their respective lives issued by the Ajax Mutual Life Insurance Company of New York, each for ten thousand dollars ($10,000), that on the life of the said John Doe being numbered 123456, and that on the life of the said Richard Roe being numbered 123457, and have deposited said policies with the said trustee; and whereas it is intended that each of said parties insured shall hereafter take out insurance from time to time in equal amounts, so that so far as possible the total amount of insurance on both lives shall always equal or exceed the value of all the shares so deposited.

Now, therefore, it is hereby agreed that the said trustee shall hold all the policies and certificates of stock deposited with it without any obligation of any nature in respect thereto other than the safe-keeping thereof and the carrying out of the provisions of this agreement at the time of the death of either of the parties of the first part, or upon the earlier termination of the trust as hereinafter provided, and upon the death of the said John Doe or the said Richard Roe, whichever event shall first oc-

cur, shall collect the proceeds of the policy or policies on the life of such decedent held under this trust and shall pay the same, together with any additional amounts collected by the said trustee, as hereinafter provided, from the survivior of the said John Doe and the said Richard Roe, to his executor or administrator and shall at the same time deliver to such survivor all the certificates of stock so held in trust and redeliver to him the policy or policies on his life held under this trust and shall release to him in writing all interest as beneficiary thereunder.

The said trustee shall pay over such proceeds as above directed, even if they exceed in amount the value of aforesaid. If, however, such value shall exceed the amount of such proceeds the survivor of the said John Doe and Richard Roe, before being entitled to receive said shares, shall pay over by the said trustee, together with such proceeds, as above provided, to the executor or administrator of such decedent.

If the parties in interest shall not be able to agree as to the value of the shares of such decedent such value shall be fixed and determined by two appraisers, one to be chosen by

such survivor and the other by the executor or administrator of such decedent; provided, that if the two appraisers so chosen are unable to agree they shall thereupon select a third appraiser and the finding of any two of the appraisers as to the value of the decedent's shares shall be conclusive and binding upon all persons.

The said John Doe and Richard Roe hereby mutually agree that each of them will punctually pay all premiums becoming due on the policy or policies on his life held under this trust, all distributions of surplus under each policy to be applied to reduce the premiums thereon.

In case of the lapse of any of such policies for non-payment of premiums while this agreement is in force, or in case of the revocation of this agreement by written notice given by both the said John Doe and Richard Roe to the said trustee, this trust shall terminate and the trustee shall return said certificates and all such policies to the parties depositing them, respectively, and shall release in writing all interest as beneficiary under said policies for a cancellation fee of twenty-five dollars ($25).

The said trustee shall be entitled to a charge of two per cent (2%) on the proceeds paid over by it to the executor or administrator or such decedent.

IN WITNESS WHEREOF the said John Doe and the said Richard Roe have hereunto set their hands and seals and the said trustee has caused these presents to be executed by its duly authorized officers and its corporate seal to be hereunto affixed the day and year first above written, in triplicate.

_____

_____

BROADWAY TRUST COMPANY

(Corporate Seal) By _____

CASH VALUES

If the corporation is the beneficiary under the policies the cash values become a quick asset of the corporation. On the other hand, if the policies are payable to individuals or to a trustee the cash values belong in accordance with assignments or other limitations *expressed* in the policy itself. As mentioned in the paragraph on "Agreements," when one party dies there will be (after the sec-

ond or third year) cash values on the policies of the survivors. It should be known in advance what will happen to these values when the first man dies.

TAXATION

The premiums paid upon life insurance for a stock liquidation fund are not a deductible expense in the Federal income tax return of the premium payer. It makes no difference whether the premium payer be the corporation or whether the premiums are paid by individuals in a stock purchase plan of their own. However, under neither plan need the proceeds of the policy be declared as income provided the insurance has matured at death and that there has been no transfer of the policies "for a valuable consideration."

The question of estate and inheritance taxes will depend entirely on who pays the premiums, and who is the beneficiary under the policy. If, for example, the corporation pays all the premiums and is the beneficiary of the policy, the proceeds, as such, payable at death, would not be subject to Federal estate tax. If, however, the payment increased the assets of the corporation, this increase might, in some circumstances, increase the value of the insured's stock when appraised for

tax purposes. On the other hand, if the estate of the insured were named as beneficiary, and the policy were paid under the terms of an agreement which provided that the insurance constituted the purchase price of the stock, it seems probable that, in most cases, the Federal estate and State inheritance taxes would be based on the value of the insurance; in other words, the tax situation would usually be the same as though the stock held by the insured had been sold at the time of his death for a price equivalent in amount to the insurance. There are so many ways in which plans for the purchase of stock may be arranged, that any very complete outline of the situation which might arise would be out of the question. However, in all transactions of this kind, the attorneys for the corporation should prepare the agreement providing for the transfer of the stock and they will be in a position to advise their clients as to the effect on taxes of the plan which is suggested.

Examples

The ideal execution of the stock purchase plan by life insurance is by a "man-to-man agreement." This avoids complications with the corporation which exists as a separate entity. It also avoids

misunderstanding by the various heirs to each man's property. It expedites the transaction at a time when a prompt settlement will be greatly appreciated, and thus places all survivors in a position to go forward with very little lost energy.

Three men, Jones, Smith, and Brown, own the Beacon Manufacturing Company. Each man has received an equal share in the profits and stock of the business. Each man has contributed his share to the development of the company since the day when they all started off together in the venture.

One day they stumble upon a discussion of each other's succession in the company if one of their number should die. This is the first time they have ever considered this very important problem as affecting them. Jones has already been approached by a life insurance underwriter with the suggestion that the Beacon Manufacturing Company draw up a business will and supplement it with life insurance.

The underwriter is invited to present his proposal for their consideration. The fundamental points in this proposal are:—

1. Immediate determination of the book value of the stock.

2. Purchase of life insurance on each man in an amount equal to his stock interest.

(a) Premiums to be paid from a pool created by *equal* contribution from the personal funds of each man.

3. The appointment of a trustee to act for the survivors.

4. The execution of a written agreement as the means to the satisfactory completion of the proposal.

Jones, Smith, and Brown liked the idea but there were two immediate obstructions. First, Smith and Brown did not have ample personal funds to contribute their share of the premium. Second, Jones was believed to be uninsurable. The life insurance underwriter met the first obstacle by suggesting an increase in salary of an amount equal to the share of premium due from Smith and Brown. This was found to be an allowable and possible procedure, and was accepted.

What to do about Jones' physical condition? No physical examination had been made but during one of the conversations it was suggested that Jones be included in all agreements except that he should be required to furnish a long term settlement by notes if necessary in return for his stock interest. However, upon examination it was discovered that Jones was insurable on a sub-standard or "rated-up" basis, so he was promptly in-

cluded as a normal participant in the agreement. The insurance and stock were made over to a trustee and the corporation's lawyers drew up the agreement binding all parties and their estates.

An example may also be cited of a case where there is no trustee and where the policies are paid to the corporation, and the premiums are paid by it.

In this instance the corporation may be contracted to use the policy proceeds to purchase the stock interest of any party to the agreement. But, it should always be remembered that the chief deterrent to this method is the fact that as soon as a policy claim is paid to the corporation at death those proceeds are available to all creditors of the corporation. Their demands may have to be met from this fund. Thus, the very purpose for its creation is defeated and its effectiveness lost.

Hence, the previous example of the Beacon Manufacturing Company has been called the "ideal" method. Furthermore, business men should be reminded that when a corporation is the executor of such an agreement, the stock purchased by life insurance funds belongs to the corporation as such and it cannot be the property of the individuals except on the basis of stock dividend or a liquidation of the company.

PARTNERSHIPS

CHAPTER VII

PARTNERSHIPS AND LIFE INSURANCE

"Partnership is the result of a contract between two or more competent parties to combine their money, property, skill or labor for the transaction of some lawful business for profit." [1]

There are four kinds of partners who may combine one with the other to form a partnership, or two or more of the same classification may combine to form a partnership. These are general, limited, dormant, and nominal. Partnerships themselves may be subdivided into general, trading, non-trading, special, limited partnerships, and a more or less antiquated form of partnership organization known as the joint stock company. This latter form is a mixture of the corporation idea with the partnership idea inasmuch as partners under this form of agreement are able to transfer their interests as though they were doing it on the basis of stock certificates.

Referring to Conyngton on "Business Law" it

[1] *Business Law*, by Conyngton, p. 339. Vol. I.

is found that "a *general partnership* is the usual partnership form for the continued prosecution of some general line of business. It is the commonest form of partnership. . . . *Trading partnerships* include all those formed for the purpose of buying, selling, or manufacturing. *Non-trading partnerships* do not buy, sell, or manufacture as a principal feature of their business. These partnerships include professional partnerships, firms of brokers, etc. A *special partnership* is formed for the transaction of some single piece of business or for the conduct of some one line of business. . . . It is to be noted that a special partnership means one undertaken for a special business, while a special partner simply means a limited partner. A *limited partnership* may be formed only under special statutes. It differs from the ordinary partnership in that certain of its partners are silent, or inactive, and the liability of these partners is limited to the amount actually invested by them. These partners are called special partners."

Further consideration or discussion of the partnership form of doing business would involve a comprehensive legal treatise on the subject. The references included above give a general idea of what business organizations might be considered

as partnerships, and if they may be partnerships under what classification they would come.

The essential point to be remembered in considering life insurance as applied to partnerships is the fact that dissolution of a partnership invariably follows the death of any partner. This is obvious because a partnership is an organization of personnel and nothing more. Consequently, in the following discussion much stress will be laid upon the inevitable necessity of life insurance in practically every partnership, the only variable being the actual definition of the need which is to be protected, together with the form of protection to be applied.

CHAPTER VIII

CREDIT REINFORCEMENT

The average partnership must give much more consideration to credit reinforcement than the average corporation. By the very nature of partnership organization credit is exposed to impairment by the hazard of death. In a corporation, credit may be momentarily suspended as the result of an executive's death, but it can be stabilized more readily because of the perpetuation of the corporation as such. In a partnership it will be impaired as the result of a partner's death and it is very difficult to stabilize it. The partnership is, of course, dependent upon its personal attributes, whereas a corporation strives to minimize the personal equation. With this fact in mind, consider the necessity of reinforcing the partnership's credit standing in every possible way.

Life insurance payable to the partnership for any purpose whatsoever will be available at all times to creditors, agreements to the contrary notwithstanding. Partners who have arranged a settle-

ment of life insurance proceeds to accomplish a "liquidation" or a "direct compensation" should be warned that these plans may never materialize regardless of agreements, if creditors need the proceeds of those policies. Consequently, the first consideration in a well-ordered partnership program should be to include ample life insurance proceeds with which to satisfy creditors if such satisfaction is necessary when any partner dies.

Any life insurance plan which may be executed between partners as individuals will be assailed in the same manner because all partners (unless limited or special) are liable to the extent of all their assets. And, this liability cannot be waived by an agreement or trust unless perhaps it is with full knowledge of any and all creditors of the partnership.

There is really no way to apply funds to special uses unless creditors' claims are to be adjusted in advance. The creditors are entitled to settlement and by due process of law it can be obtained. Insurance should be carried on the lives of all responsible parties to assure the completion or dissolution of any credit obligation.

Furthermore, substantial creditors of any partnership should make it their business to know that their interests in any partnership are amply pro-

tected in the event of any responsible partner's death. This is their right and they should curtail or refuse credit until evidence is given that their claims can be liquidated on demand at the time of a death.

Of course, the dispatch with which life insurance policies provide the necessary capital recommends it as the most efficient medium to be used.

AMOUNT OF PROTECTION

The amount of protection should be an amount equal to the average "per-partner" responsibility over a period of years. If a three-man partnership's maximum obligations during any year amount to $250,000, and the minimum obligations $50,000 their average floating debt is $150,000. This would call for approximately $50,000 on the life of each of the three partners. These amounts may be varied if the partnership is carrying any form of "direct compensation" by life insurance. It will be readily seen that as large an amount of "credit reinforcement" will not be necessary when the direct compensation proceeds are apt to include a partial allotment for the use of credit stabilization. The two factors overlap slightly, and this fact should be taken into consideration

when estimating the necessary amount of insurance.

POLICY FORMS

Ordinary and limited payment life policies may be used as the need requires.

If, by any chance, the period of obligation is definite, a limited payment life policy may be used unless the lives to be insured are too advanced in years to make this form advisable. The net cost will make a favorable comparison with ordinary life where the period of protection is limited, plus the fact that if at the expiration of the known period it seems advisable to continue the protection the policies are paid for and may be continued as such.

On the other hand, if the extent of the obligation cannot be measured in terms of years, ordinary life is the more adaptable.

In all cases term or modified life insurance may be used if this form of "leased" protection is to the advantage of the clients.

PREMIUM PAYMENT

The partnership itself should assume the payment of all premiums for policies the proceeds of

which are to be applied to the reinforcement of credit. It is possible that the creditors might feel it necessary to pay the premiums themselves especially if the financial condition of the partnership at the time the insurance was needed was such that it would not permit the additional outlay.

BENEFICIARIES

The beneficiary should be the estate of the insured, but the policy should be immediately assigned to the partnership as soon as it is put into force. This may seem to be a roundabout method of reaching a simple end. It is a more secure provision than to name the partnership as the irrevocable beneficiary even though the latter procedure can be followed. If, as suggested in the paragraph just preceding ("Premium Payment"), the creditor does assume the obligation of premium payment all beneficiary rights should be assigned to the creditor immediately by a collateral assignment.

ASSIGNMENTS

The first assignment suggested in the preceding paragraph should be an "absolute" form. The insured has no immediate right or title to the policy or its values when an assignment is in

force. For that reason its benefits must accrue completely and totally to the partnership or to the creditors as the case may be.

Some companies may provide a special beneficiary clause for a partnership which would make an absolute assignment unnecessary.

When the partnership finds it embarrassing to pay premiums and the creditor assumes that obligation the assignment is executed on a collateral basis. This form is used because the partnership still has some rights under the policy by virtue of its previous premium payments. If, for some reason or other, the creditor has paid for the insurance since its inception that creditor's ownership of the policy should be on the basis of an absolute assignment.

AGREEMENTS

An agreement for effecting credit reinforcement would be superfluous. It could not control the order or manner of satisfying the creditors, as that procedure is controlled by law.

CASH VALUES

As the policy is assigned so belong the cash values. All right and title to the assets are carried by the assignment and they cannot be shown or

declared as assets by anybody but the assignee. The insured should never have any right to them, unless the policy is surrendered to him at some time or other for value received.

TAXATION

Premiums paid by a partnership for credit reinforcement are not a deductible item in making Federal income tax returns. In this connection it is important to remember that a partnership, as such, is not a taxpayer. An informational return is filed by the partnership but the individual partners are actual taxpayers who, for tax purposes, report their share of the partnership income on their individual returns.

In a special case, the Federal tax authorities ruled that when one of the members of a partnership was required to take out life insurance in favor of the other partners in a business venture in order to retain them as partners, the premiums might be deducted by the taxpayer (partner) as a business expense provided the proceeds of the policies, if paid, would not be used in satisfaction of any obligation of the taxpayer. This ruling covers only a specific case, however, and it does not seem probable that the Federal tax authorities

would allow this deduction in the average case where a policy is taken to protect the interests of surviving partners. Of course, if the insured would benefit directly or indirectly from the payment of the proceeds to the surviving partner, no deduction would be allowed.

There is no Federal income tax on the proceeds of a policy of this kind payable at death unless the beneficiary acquired the policy by assignment or otherwise for a valuable consideration.

The question of Federal estate taxes and State inheritance taxes will depend largely on who pays the premiums. If the insured has paid no portion of the premiums, directly or indirectly, no Federal estate or State inheritance taxes would be levied on the proceeds at the death of the insured. However, if the insurance is payable to a named beneficiary other than the insured's estate and the insured has paid a portion of the premiums, the Federal tax authorities will consider that he has taken out the insurance in the proportion that the premiums paid by him bear to the total premiums paid. Most States do not tax the proceeds of insurance when paid to a named beneficiary other than the insured's estate regardless of whether or not the insured has paid the premiums, but if your State does tax insurance proceeds payable

to named beneficiaries you should study carefully the rulings for the tax question is bound to come up in a case of this kind.

Example

Two men in an Eastern city had formed a partnership some years ago for the purpose of transacting a wholesale produce business. One man was fifty-three, and the other was forty-nine, and they had been in partnership for approximately fifteen years without ever having given a thought to business life insurance. Over that period of time they had been successful and had accumulated an estate of reasonable size. The subject of life insurance was first mentioned to them in an off-hand way, but it soon developed that there was every reason in the world for them to consider seriously the establishment of some fund which would liquidate their credit obligations at the time either one should die. When their attention was called to that fact both agreed that the sudden death of either would cause considerable embarrassment irrespective of the amount of available cash at that time. The primary reason for this conclusion was the fact that they carried a large line of credit at the bank to cover shipments from the Far West and Florida. Their credit was good

and the bank had never questioned the necessity of life insurance inasmuch as there was ample collateral to offset any loan which was made. However, it seemed very reasonable to the two partners that in event of the death of one, the survivor should have sufficient cash to liquidate all outstanding obligations, thus making it possible for him to give his attention solely to the marketing of his perishable merchandise. In addition, each partner was asked to picture himself as the survivor, and in that light each man readily visualized how very much alone he would be if the other should die. No time could be taken for credit readjustment unless it were to be done automatically, which is to say by life insurance. The result was $35,000 on the life of each partner. Each man mentioned the other as his beneficiary, revoking the right to change that nomination. They elected this method of settlement because both agreed that there was no reason why the deceased partner should have any share in the proceeds of the policy except as such proceeds might indirectly enhance his share of the partnership. In order to avoid any complication, their lawyer prepared a short and very simple document which in substance stated that the estate of the first deceased partner would surrender to the

survivor such rights as he might have in the policy outstanding upon the life of that survivor. It was further stated why the insurance had been taken and for what purpose the beneficiary was obligated to use the proceeds.

CHAPTER IX

LIQUIDATION FUND

The next thought which comes into the mind of a life insurance underwriter when considering a partnership from his point of view is that he must supply a liquidation fund for the settlement of any deceased partner's interest in that partnership.

It has been pointed out that a partnership must be liquidated in the event of the death of any partner. This means that the law will demand a complete and immediate liquidation of the deceased partner's interest and any enforced delay is very much to the disadvantage of all concerned. Life insurance is presented as the best solution to this very vital problem with which all surviving partners are confronted. It is another instance of life insurance being "a known method of providing for the known need at an unknown time." Surviving partners are placed in the very fortunate position, if they have carried insurance on the life of their deceased partner, of being able to

settle all accounts with the estate, and thus prevent momentary or prolonged suspension of their business, or interference on the part of the executors of that estate, and their working capital is left unimpaired at a time when they will undoubtedly need it all.

This very naturally brings us to a discussion of the ways and means of properly applying life insurance as a liquidating fund in the working agreement of any partnership.

AMOUNT OF PROTECTION

It is ordinarily very easy to determine the amount of protection necessary in order that a partner's interest may be liquidated at the time of his death. When life insurance is applied against this need all partners participating in the plan should determine the book value of their interests by a mutually satisfactory method. The amount of protection should exactly equal the value of each partner's interest as of the day that such an appraisal is made. It should be pointed out immediately that such an appraisal should be executed as often in the future as any partner may feel that his interest is undervalued. In other words, the life insurance should be made to equal

at all times the value of the interests which it is supposed to liquidate. If this is not done it means that additional financing will be necessary when the amount of insurance is inadequate for the outright purchase of the interest. Partnerships should understand this point very clearly as many cases have been so carelessly executed that the workability of the insurance plan was considerably impaired. The life insurance underwriter responsible for the execution of his client's business should not hesitate to approach every partnership regularly in order that he may ascertain the current effectiveness of his insurance plan. Partnerships for their own good should willingly cooperate with that underwriter in maintaining an adequate line of life insurance.

POLICY FORMS

Ordinary life insurance is the best medium of protection for the average partnership case. At its inception a partnership may very well carry term or modified life insurance pending its ability to meet the premiums necessary for ordinary life protection, but in no case should a partnership continue to carry term insurance any longer than is necessary. Endowment insurance may also be

used if it is possible to have a mutual understanding that any or all of the partners will wish to liquidate their interests prior to their death at a date specified in advance. The execution of this specification may not be carried out when the date arrives, but the money is there if it is needed. This form of liquidating a partnership interest is very desirable if the partners are able to determine some anniversary date upon which they wish to effect their retirement.

PREMIUM PAYMENT

The question of premium payment involves more arguments than any other phase of life insurance as applied to partnerships. The perennial problem of taxation as it enters into the arrangements of premium payment will be discussed later. Here the discussion will be confined to the basic reasons for one or another of the methods of paying the premiums. If the partnership were to pay the premiums on all policies the insurance would be payable directly to the partnership as such, which would mean that the deceased partner's interest would include his share of the policy proceeds. It would further include his share in the

cash value on the policies of the surviving partners. These two disadvantages, unless specifically eliminated by mutual consent, would tend to rule out the idea of having the partnership pay the premiums. The ideal arrangement is to have the total premiums pooled and split pro rata as a personal and private obligation among all partners participating in the insurance agreement. This might be varied slightly to such an extent that each partner should participate in the premium payment on all protection except that upon his own life. The latter method would be of interest in those cases where there is a marked discrepancy in the ages of the partners and high amounts of their interests. A further suggestion might be made, namely, that each partner pay the premiums on his own insurance, making it payable to his associates. This arrangement would be advantageous if it were desirable to avoid complicated bookkeeping, or if each partner were anxious to be fully informed as to the status of his own policy. There is one additional procedure and that is the use of a trustee as a medium for premium payment, and as a medium for settlement. This will be dealt with in a subsequent paragraph entitled "Trusts."

BENEFICIARIES

The discussion of premium payment just preceding leads directly into a consideration of the election of beneficiaries. If, in an exceptional case, the partnership pays the premiums it should be nominated as the irrevocable beneficiary in order that the most efficient and equitable distribution of the proceeds may be made. But, if this be the procedure it should be remembered that the proceeds from the deceased partner's life insurance have enhanced the value of his share in the partnership in direct ratio to the size of his participation. Provision to obviate this development should be made by a clause in the life insurance agreement such as paragraph 3 on page 156. However, if the premiums are to be paid out of a personal pool each partner should name his associates as the beneficiaries insofar as their several interests may be represented in the proceeds of the policy.

The beneficiary should be irrevocable if the insurance is carried on one life and the premiums are paid by the associates, or if the insurance is carried by each partner on his own life in favor of his associates. Under these beneficiary clauses all partners are protected against fraud or ignorant manipulation of the policy or its assets. Each

beneficiary thus reserves unto himself the right to know what each insured is doing with the policy at all times, as no alteration or deduction may be made by the insured without the consent of the beneficiaries.

It should be fairly obvious, in view of the objections and recommendations just cited, that the most efficient way to execute a partnership liquidation is a party-to-party plan without involving the partnership as such. A trust created by the partners as individuals will provide the desired results. In this instance, the trustee would appear under deed of trust as the beneficiary in the policy and the proceeds could then be distributed as directed.

ASSIGNMENTS

The use of assignments in partnership insurance is most infrequent because, as has been explained in the preceding paragraph, the use of an absolute or irrevocable beneficiary as named in the policy affords ample protection to those beneficiaries who have an actual interest in the policy. An assignment affords an ironclad policy contract in behalf of the assignees, but it is not recommended that any partnership should use an as-

signment without discussing the subject thoroughly with the legal department of the insurance company issuing the policy contract.

AGREEMENTS

It is essential that all partnerships should use a life insurance agreement with their protection. Such an agreement may well be embodied in their actual articles of partnership. It should be drawn by the partnership's own attorney, but at his pleasure he should have the coöperation of the underwriter on the case and the legal department of the insuring company. There follows an example of a partnership agreement which was used in a specific case. It is not to be considered as a "form" agreement applicable to any and all partnership cases. It is merely cited in order that it may show some of the salient points which should be covered.

Example 1

THIS AGREEMENT, made this —— day of ————, 1927, by and between John Doe, of New York, N. Y., and Richard Roe, of New York, N. Y. WITNESS THAT

WHEREAS, the said John Doe and the said

Richard Roe have entered into a partnership under the firm name of Doe & Roe, and

WHEREAS, the present valuation of the said business is approximately fifty thousand dollars ($50,000), and

WHEREAS, it is the desire of the said partners to protect each other from loss by reason of the death of either of them, and for this purpose each has caused to be issued upon his life a policy of life insurance in the Ajax Mutual Life Insurance Company, Policy No. 123456 for twenty-five thousand dollars ($25,000) being issued on the life of John Doe payable to Richard Roe, and Policy No. 123489 for twenty-five thousand dollars ($25,000) being issued on the life of Richard Roe payable to John Doe;

NOW, THEREFORE, THE PARTIES HERETO AGREE AS FOLLOWS:

1. The first and all subsequent annual premiums for each of said policies shall constitute a charge against the partnership funds and shall be paid by the firm when due.

2. In case of the death of any of the partners, the amount, if any, payable to such deceased partner's personal representatives as his share of the partnership assets, shall

be ascertained as hereinafter provided for, and in consideration of the payment of the said annual premiums out of the partnership funds, the surviving partner does agree to use the proceeds of said policy of insurance in making settlement for the amount due as shown by the said account.

3. It is agreed that the valuation of the business as of January 1, 1927, is fifty thousand dollars ($50,000), and it is further agreed that upon the death of any of said partners, the survivor does agree to purchase from the estate of the deceased the interest of such deceased partner at the time of such decease, the price to be fixed by a physical inventory, to be taken within ten days after such decease, and to use for said purchase the proceeds collected from the policy of insurance on the deceased partner's life, such inventory not to include the amount paid by the insurance company under the deceased partner's policy.

4. The deceased partner agrees for himself, his heirs, executors, and administrators, that he will sell to the surviving partner his interest for the amount of the valua-

tion as fixed by such physical inventory.

5. It being the purpose of this agreement that the proceeds of the insurance policy on the deceased partner's life shall be used in purchasing the interest of the deceased partner in the business, it is further agreed that the amount of the deceased partner's interest in the business which is in excess of the amount received from the insurance company shall be paid forthwith to the deceased partner's personal representatives.

6. It is further agreed that if the amount of the deceased partner's interest in the business is less than the amount received from the insurance company, the excess shall nevertheless be paid to the estate of such deceased partner.

7. It is further understood and agreed that in case of the dissolution of said partnership during the lifetime of both of said partners, the above policies shall be considered as assets of the partnership. The outgoing partner has the right to retain the policy on his own life, PROVIDED that he pays to the remaining partner his share of the cash surrender value of such policy.

8. This agreement shall be binding upon the heirs, executors, administrators of the parties hereto.

In witness whereof, the parties hereto have set their hands and seals, this —— day of —— 1927.

Witnesses:

———————— (signed) John Doe (seal)

———————— Richard Roe (seal)

If the original partnership agreement contains a provision for winding up the business in case of a partner's death, it should be amended to make it accord with the Supplemental Partnership Agreement, which, through the use of life insurance, provides for a continuance of the business by the surviving partner.

It should be noticed that the agreement shown above provides for premium payment out of partnership funds. To offset it, as was pointed out in the paragraph "Premium Payments," the partners contract for their estates that their interests in the policies shall be relinquished each unto the other according to a previous understanding.

Consequently, this specimen agreement should be borne in mind as a guide in cases where it is desired to make premium payments out of partnership funds, even though it is recommended that such a procedure be avoided.

If the policy proceeds are to be paid direct to the beneficiaries the only statement that should appear in writing, and that is hardly essential, is the fact that each partner covenants on behalf of his estate to settle with his survivors on the basis of the life insurance proceeds as a minimum amount in exchange for his interest. Take an example which will demonstrate this point. "The interests of three partners, A, B, and C, are appraised at $25,000 apiece on the first day of January, 1926. Life insurance is taken on each life in the same amounts, A's policy payable to B and C, B's policy payable to A and C, and C's policy payable to A and B. On July 15, 1926, one partner, B, dies. An appraisal is made of his interest which shows his share to be worth only $20,000. The understanding is that his agreement previously entered into with A and C would mean that those survivors will be obliged to pay his executors the full $25,000 according to their previous agreement." Other clauses to appear in the agreement should include a definition of the policies taken,

together with the method of premium payment elected. Other details may be added at the discretion of the attorney and the partners involved.

TRUSTS

It is conceivable that a partnership might desire to execute the liquidation of their several interests through the medium of a trusteeship. The trustee may be a fiduciary institution incorporated for the purpose of executing such a trust, a personal trustee, or a combination of the two. The powers of such a trust would naturally be clearly defined in a deed of trust to be drawn in behalf of all parties concerned. Its advantages might be summed up by saying that it removes the necessity of transacting frequently undesirable business by individuals. In other words, it removes the personal element which might handicap those concerned. The trust may be empowered to pay the premiums and collect the proceeds and effect the liquidation. This is a modern development in the use of a trustee, and if a partnership works in close association with its bankers it is recommended that they consult the trust officer of that bank relative to the suggestion made here. It has been impossible up to the present time to secure a

copy of such a trust actually in operation, although it might be possible to use the following memorandum of agreement which was originally drawn for a corporation.

Example 1

THIS MEMORANDUM OF AGREEMENT by and between John Doe, first party; Richard Roe, second party; and the Broadway Trust Company in its capacity as Trustee; WITNESSETH THAT:

WHEREAS, the said John Doe and the said Richard Roe have entered into a partnership under the firm name of Doe & Roe;

NOW, THEREFORE, it is agreed that in consideration of the covenants hereinafter contained, and the payment to the Trustee herein of One Dollar and other valuable considerations by each of the first and second parties, the receipt whereof is hereby acknowledged, and in further consideration of the issuance of two policies of life insurance upon the life of each of the two parties payable to the Trustee herein, and the payment of the premiums thereon equally by the said first and second parties;

IT IS AGREED that the said John Doe, party

of the first part, shall be insured in the sum of twenty-five thousand dollars ($25,000); and Policy No. 1234578 of the Ajax Mutual Life Insurance Company, has been duly issued upon said first party, and the amount due under the policy at the decease of the said insured, John Doe, shall be paid to the Broadway Trust Company, as Trustee. And in the event the insured shall survive the Trustee, then all right, title, and interest in and to the said policy shall revert to the insured as per Section 4.

It is agreed that the said Richard Roe, party of the second part, shall be insured in the sum of twenty-five thousand dollars ($25,000); and Policy No. 124590 of the Ajax Mutual Life Insurance Company, has been duly issued upon said second party, and the amount due under the policy at the decease of the said insured, Richad Roe, shall be paid to the Broadway Trust Company, as Trustee. And in the event the insured shall survive the Trustee, then all right, title, and interest in and to the said policy shall revert to the insured as per Section 4.

First: The Trustee surviving shall, upon the death of one of the said parties, receive

the proceeds of the policies upon the said life, and for that purpose shall have full power to collect the same and execute and deliver any receipts and vouchers for the same.

SECOND: It is agreed by and between the said parties hereto that the interest of the first party shall be valued at a minimum of $————, and the interest of the second party at a minimum of $————. If, however, the executors or administrators of the estate of the deceased partner believe this total value of the deceased partner's interest in the said partnership to be in excess of $————, then the price to be paid shall be such as may be agreed upon between the survivors of the said partners and the said legal representative of the estate of the deceased party.

If, however, no agreement can be reached by such parties, then the value shall be fixed and determined by two appraisers, one to be chosen by the surviving party, and the other by the executors or administrators of the deceased party, and the value of the interests as determined by these appraisers shall be final and binding upon all persons, provided that if the two appraisers so chosen are un-

able to agree, they shall thereupon select a third appraiser, and the finding of any two of the appraisers shall be conclusive and binding upon all persons.

THIRD: The said party surviving, acting as Trustee, shall pay to the estate of the said decedent the total amount due under the said policy on said decedent's life. If the net proceeds of the aforesaid policy upon the life of the decedent shall, by reason of borrowing or other diminution, be less than $————, or the appraised value of the decedent's interest shall be found to be greater than $————, then the transfer and sale shall be consummated of such proportionate share of the interest of the decedent partner as the said insurance proceeds will purchase at the said established or appraised value, the balance of the appraisal price to be obtained and transferred from some other source to be determined at the will of the survivors when such transfer is necessary.

FOURTH: While the policy on the life of either John Doe or Richard Roe, whoever first deceases, shall be used as aforesaid, it is agreed that on the death of said first deceas-

ing party, all right, title, and interest in the remaining policy upon the life of the survivor shall be released and transferred to such survivor free of all trust by the executors or administrators of the deceased without any consideration whatever being paid therefore by the said survivor. The said survivor may use the said insurance on his own life for personal or family insurance or otherwise as he may choose.

FIFTH: The policy of insurance on the life of John Doe shall be delivered to, and held by the Broadway Trust Company, Trustee as aforesaid, together with a copy of this agreement filed therewith.

The policy of insurance on the life of Richard Roe, shall be delivered to, and held by the Broadway Trust Company, Trustee as aforesaid, together with a copy of this agreement filed therewith.

This agreement shall be binding upon our executors, administrators, or assigns.

IN WITNESS WHEREOF, the parties hereto set their hands and seals this —— day of ————, 1927.

———————————— First Party

Individually and as Trustee as aforesaid
——————————— Second Party
Individually and as Trustee as aforesaid

It is repeated for the sake of emphasis that this is not a working trust agreement, but is merely a revised corporation memorandum of trust which is cited in order that it may suggest some ideas which might be used in the creation of a partnership trust. It is further repeated that no underwriter should endeavor on behalf of his clients to prepare such a deed of trust, but that he should refer the matter entirely to the attorney for that partnership and the trustees whom they may elect.

CASH VALUES

If the beneficiary clauses are provided according to the several examples cited in the paragraph "Beneficiaries" the cash values would be the joint property of the insured and the beneficiaries. However, in no case can the cash value be disturbed by either one or the other without mutual consent. In this way the cash value becomes an asset in name only for neither one nor the other can consider it his own. However, if an assignment is used the cash value, as has been pointed out in a previous paragraph, will be the

property of the assignee under a collateral assignment to such extent as the interests of the assignee may appear, or under an absolute assignment they will be the sole property of the assignee.

TAXATION

It seems inevitable that in every case of partnership insurance there is an ambition to put life insurance premiums in the category of "legitimate expense" of the business for Federal income tax purposes; that is, for some reason the question of premium deduction seems to come to the fore more in the discussion of insurance for partnerships than in the discussion of insurance for corporations, although there is possibly even less chance that a deduction of this kind will be allowed in the case of a partnership. The fact cannot be repeated too often that under present rulings no premium on life insurance can be deducted as expense on Federal income tax return if it can be successfully shown that the proceeds of the policy revert directly or indirectly to the benefit of the taxpayer.

As far as estate and inheritance taxes are concerned, no tax will be levied against the estate

of the deceased partner if the premiums have actually been paid by persons other than the taxpayer and the proceeds of the policies are paid to those premium payers. The taxpayer's estate will be taxed under inheritance and estate tax laws on the basis of the settlement which is executed between his surviving partners and his executors or beneficiaries.

Example

A short while ago three men entered into a partnership agreement for the transaction of a brokerage business in listed stocks and bonds. Two of the men were brothers and both were older than the third. All of them, however, had had previous experience in this business. Each of the three had demonstrated particular adaptability to some special phase of the work. For purposes of identification let us call the two brothers A and B, and the other member of the firm shall be known as C. A, the principal factor in the partnership, had been particularly successful in obtaining participation in bond issues which were marketable and current, and owing to the fact that the partnership early decided to pursue some activity along this line, it was decided that A should be given

this work to do. B had obtained most of his experience as an inside man. He knew accounting systems as applied to brokerage houses, and he also knew the intricacies of stock and bond transfers in addition to having an intimate knowledge of handling margin accounts. C had always been active on the outside, but primarily as a retailer engaged in distributing bonds to the small buyer, and soliciting stock trading accounts. So, as in the case of A, both B and C were designated to supervise that phase of the work in which they had had previous experience.

A and C had both worked for the same company prior to forming their own partnership, and due to peculiar developments within that old association they had to move to their new situation as the result of a sudden decision. Their capital was accumulated in a helter-skelter manner in order that they might be in a position to do business as soon as possible. It is not known to what extent each member contributed cash to the partnership, but it is known that A supplied the Stock Exchange membership at a cost of $145,000. Shortly after the partnership had been formed a life insurance underwriter suggested the necessity of life insurance in the event of death of any of the partners in order that sufficient funds might

be available to liquidate each partner's interest and thus avoid the possibility of suspending activity in their business. It is easy to see that the hazard of suspension would be very much greater if A died than with the other members because of the necessity for obtaining his seat on the Stock Exchange. Investigation revealed the fact that all partners were in the process of reimbursing A for his Stock Exchange membership in such a way that it would comply with all regulations of the Stock Exchange as far as ownership was concerned. This point is explained because they were shortly on a basis of share and share alike distribution of any profits in the partnership. After discussing the situation in as much detail as possible the life insurance underwriter proposed $75,000 each on the three partners with an added policy of $100,000 on the life of A, this additional amount being necessary in order that they might actually buy back the Stock Exchange membership. All policies were made payable to the two possible survivors, but the partnership undertook to pay all premiums.

In the event of a death the proceeds will be distributed according to an agreement which they have all entered into with the trust officer of their bank. The three policies of $75,000 were on an

ordinary life basis, but owing to the limited working capital and lack of profits it was necessary that the additional $100,000 on A's life should be five year term insurance.

CHAPTER X

DIRECT COMPENSATION

A partnership, even more than a corporation, needs some source of direct compensation to atone for the economic loss of a human asset in that partnership. The actual partners in the business are invariably such vital factors that to lose either or any one of them would entail an actual financial loss to the partnership.

Those responsible for the development, execution, and maintenance of the business all represent insurable interests.

Subsequent consideration will be given to the different classifications into which each unit may fall, but in general it should be noticed that a partnership security is always jeopardized by a death, and the demand and need for quick financial compensation is much more necessary than in a corporation under similar circumstances. This applies to employees of the partnership as well as to the actual partners.

Partnerships exist today which are virtually

corporations except for the absence of a corporation charter and the existence of some comprehensive partnership agreement. The classification as given under "Partnerships and Life Insurance" explains the composition of the various combinations of partners. It is advisable in every case for a life insurance underwriter to ascertain the contents of the partnership agreement which his life insurance will supplement, because even when life insurance is to be applied as direct compensation he should be sure that the articles of partnership are not declarations which are counter to the execution of his purpose.

The very name of direct compensation as applied to this form of life insurance settlement indicates that the proceeds are paid to the treasury of the partnership. Consequently, it is essential that a partnership agreement protected by life insurance should be drawn as explained in the preceding section of this chapter, otherwise those funds intended to be applied as direct compensation for the loss of a human asset will have to be used in the liquidation of the business (or as credit reinforcement, see page 136.

A legal opinion will often be necessary in order to determine that the funds are actually going to be available for the use intended. One ele-

mentary guide is that which has just been stated, namely, that a fund for direct compensation must be superseded by ample provisions for credit reinforcement and for liquidation of the partnership.

The Valued Employee or the Expert

Many partnerships have in their employ an expert or an employee whose special training or knowledge constitutes a very vital asset to the partnership. If this type of man dies while actively engaged in his work it will mean a financial loss. He will be a difficult man to replace, and in order to replace him time, money, and effort must be spent on his successor.

Furthermore, the partnership may have invested considerable money in the education of the deceased, and it is certainly a financial loss if they have not enjoyed complete return upon their investment.

This form of protection constitutes one of the basic considerations of the use of life insurance in business.

Its comparison to the application of other forms of insurance upon material assets is exact and conclusive. As most people know, business men often feel that they could suffer the loss of their plant

and material assets if only their human assets remain unmolested.

AMOUNT OF PROTECTION

The partnership may choose any one of the following methods to determine the amount of protection necessary in such a case.

1. Take an amount equivalent to ten years' salary for the man.

2. Take an amount equivalent to contracts, the execution of which depends upon this man.

3. Take an amount which will provide a large enough purchase price to obtain his successor in the open market.

POLICY FORM

Ordinary life insurance is recommended as the best medium of protection because the insurance has been placed to protect the partnership's interest in either or both of these cases as long as the man may live.

PREMIUM PAYMENT

The partnership should pay the premiums on policies of this kind because the partnership is the

direct and sole beneficiary of the policy. If, however, the partnership's insurable interest should cease the policy may be transferred to the insured, in which case the latter will, of course, pay the premiums.

BENEFICIARIES

The standard form of application and policy should be used. The "estate" should be named as beneficiary. This should be supplemented immediately by the execution of an absolute assignment conveying all right and title under the policy to the partnership as assignee. If a partnership shall cease to have an insurable interest in the insured, the policy may be released to the insured as his personal property upon such terms as the partnership may name, and at their discretion.

Merely revoking the right to change the beneficiary is not sufficient inasmuch as the partnership must then consult the insured at the time of any change which they may wish to make in the policy. This is neither advisable nor necessary.

ASSIGNMENTS

As stated in the previous paragraph this form of protection would require the execution of an

absolute assignment. Such an assignment conveys to the partnership all right and title under the policy as a claim at death, or during the lifetime of the insured. A collateral assignment might be used were it not for the fact that there is invariably no restriction placed upon the interest which the partnership has in the life of the insured.

CASH VALUES

The cash values are the property of the partnership if an assignment is in effect. They are available for the purpose of temporary financing if necessary. They may be carried as assets on the balance sheet of the partnership. If the beneficiary is irrevocable the cash values are the property of the partnership subject to the release of the insured.

TAXATION

The premiums paid on a policy of direct compensation upon the life of a valued employee or expert are not deductible business expense in making the Federal income tax returns of the members of a partnership.

Inheritance or estate taxes would not be levied upon the proceeds of this form of policy inasmuch

as the insured is not carrying the insurance himself, and he has no right nor title under the policy, nor would his estate receive any benefit at his death.

Example

An old-fashioned house of commission merchants had always operated as a family partnership. They had in their employ a man thirty-six years old who was virtually a jack-of-all-trades. In his own heart he was looking forward to the day when he would become a member of the partnership, which fact accounted for his diligence and willingness to work as an employee. It so happened that the two surviving partners were well advanced in years, and their attention to the business of the company was rather indifferent and scattered, but they were thoroughly appreciative of the fact that this man, who was really their office manager and cashier, represented a very vital factor in their scheme of things. The partners had a mutual friend of their own generation in the life insurance business who, after repeated efforts, finally prevailed upon them to carry an ordinary life policy of $25,000 on this employee. The proceeds were made payable directly to the partnership and the

partnership paid the premiums. The transaction was ultimately closed because the partners were definitely convinced of the fact that it would cost them that amount of money to replace and train a successor.

Contracted Parties

It is a prevalent practice for life insurance to be used in protecting that interest which a partnership may have in the lives of individuals under contract to that partnership, but not necessarily a part of it. To a certain extent this form of protection may be considered exactly the reverse of the use of life insurance as credit reinforcement, because in this instance the partnership is protecting itself against loss which may be incurred as the result of the death of any person responsible to it. Ordinarily this form of protection would be carried by the contracted parties, but in many instances the partnership itself will not have the right to demand the protection. Therefore, if the protection is necessary the partnership must carry it.

There is a very definite distinction between a contracted party and an employee or member of a partnership, so the two should not be confused in a consideration of this need.

AMOUNT OF PROTECTION

This should be based upon the part played by each individual in the execution of the contract. An amount equivalent to a minimum of fifty per cent of the contract value should be placed on the lives of those immediately responsible for the execution of the contract. This minimum figure should be enlarged if possible to equal the total amount of the contract, but it is recommended that several policies be executed so that as the contract approaches completion the insurance may be discontinued if desired, according to the incompleted value of the contract.

POLICY FORM

The form of policy to be used depends upon the length of the contract period. If that period be five years or shorter, term insurance is the best form to use. If the period be five years or longer with some doubt as to its actual duration beyond ten years modified life should be used. Lastly, if the period be indefinite or protracted always use ordinary life. Even under the first two circumstances it might be more desirable to use ordinary life provided that the figures which the life insurance underwriter presents to his client bear

out this contention. In the last analysis, the lowest premium payment form is usually demanded by the client to provide protection for this need, in which case term insurance must have preference.

PREMIUM PAYMENT

As pointed out in the introductory paragraph to this chapter, premiums must be paid by the partnership unless the contracted parties are under such obligation that the partnership may demand premium payment by them. The answer to this question will be very obvious as each case arises.

BENEFICIARIES

It is understood that in all cases the partnership should be the beneficiary if it pays the premiums. The insured must name his estate and immediately execute an absolute assignment to the partnership. If the insured pays the premiums it will be sufficient and best to name the partnership as an irrevocable beneficiary.

ASSIGNMENTS

An absolute assignment should only be used if it is necessary to execute the suggestion offered in the preceding paragraph.

This will convey all right and title to the beneficiary, which is the premium payer, leaving no access by the insured to the credits or proceeds of the policy. This is obviously just and equitable. A collateral assignment might be used if for any reason the assignee and assignor were to have a proportionate interest in the credits and proceeds. This would apply, for instance, if there was a joint responsibility for premium payment.

CASH VALUES

It should be understood that with an irrevocable beneficiary neither the insured nor the beneficiary can withdraw the cash value without the knowledge and consent of the other. This protection for the beneficiary makes it impossible for the insured to impair the value of the policy in the event of death. In other words, it would be rather embarrassing if the contracted party were to die and the partnership as beneficiary were to discover that loans had been executed on the policy to such an extent that the proceeds as a death claim were next to nothing.

TAXATION

Premiums paid by the partnership are not deductible business expenses for Federal income tax purposes.

However, if the insured pays the premiums and the partnership is vested with all rights under the policy it might come within the interpretation of the Revenue Act of 1926 that the insured could deduct the premiums as expense, provided no benefit accrues directly or indirectly to the insured in the event of his death. This deduction should be made by the insured only on the advice of his attorney.

Here again the question of who has actually paid the premiums might determine the taxability of the proceeds of the policy under State and Federal transfer tax laws. If the insured has paid no portion of the premiums on the policy payable to the partnership, no Federal estate taxes or State inheritance taxes would be levied on the proceeds at the death of the insured. On the other hand, if the insured has paid the premiums on the policy payable to the partnership, the insurance might be considered in the same light, under Federal and State laws, as any other insurance which the insured carried on his own life.

Example

A partnership engaged in buying and selling cotton had been doing business for many years in the city of Boston. Several changes had taken place in the personnel down to the point where there were three active partners who were doing business on money provided by a "silent partner" who had retired. An agreement had been entered into by all parties which stipulated that the capital provided by this silent partner would remain active in the partnership as long as he lived, in return for which the partnership gave a representative share of the profits. Prior to the actual consummation of this agreement the active partners very quickly realized that the condition of their business would be decidedly topsy-turvy if they were forced to make a sudden adjustment with the estate of the silent partner at his death. The necessity for life insurance was obvious, and the partnership immediately contracted for an ordinary life policy of $150,000 which was placed on the life of the silent partner. This amount of insurance represented within a few thousand dollars the actual amount of capital which had been supplied. The beneficiary was stated in the policy as being the estate of the insured, but that was

immediately supplemented by the execution of an absolute assignment to the partnership inasmuch as they were to be the sole owners of the policy.

Partners

Direct compensation for the loss of a partner is a vital consideration. It should not be confused with the chapter which deals with the liquidation of a deceased partner's interest in the business, nor with the chapter on the reinforcement of credit by insurance on that partner's life. It should be remembered that the law may prevent a partnership from using the funds produced by a policy of direct compensation as such, unless it has previously made provision for a liquidating fund. Consequently, a consideration here of a policy of direct compensation upon the life of a partner presupposes the existence of some fund by life insurance or otherwise with which to liquidate his interest.

As to the desirability of direct compensation in terms of money for the loss of a partner,—it is only necessary to point out that by virtue of partnership organization it is highly probable that each man possesses some particular adaptability to his particular work in the partnership. So, to

lose any partner by death means that a very vital cog has been knocked out of the wheel, and in order to insure the highest degree of efficiency after his death the business should not have to suffer a financial loss.

The deceased partner may have been responsible for a representative share of the business which might disappear entirely from the books at the time of his death. It is certain that any business would welcome liquid capital with which to tide over this embarrassment. A new clientele or a new list of customers would have to be rebuilt at an expense of time and money.

Any partnership should reckon its insurable interest in the lives of its partners. Once having established a liquidating fund, which must come first, they should provide the partnership with direct compensation in the event of the death of any partner.

AMOUNT OF PROTECTION

No formula can be used to solve this question. Each partnership will have some special gauge for determining the value of each partner's life to the partnership itself.

The volume of business for which a partner is

responsible can be a fair guide to the amount of protection. This applies only to a partnership involved in selling a commodity or a service.

The producing partner or the financial partner can only be protected according to a figure estimated by all partners and the life insurance underwriter as being a fair evaluation of the man's worth.

The amount of protection is predetermined if a partner represents a known asset to the partnership by virtue of money invested, contracts obtained, service rendered, or obligations incurred in his name. All of these considerations would represent a set figure for which the partnership should be compensated in the event of that partner's death.

POLICY FORM

Ordinary life supplies the protection in the most efficient manner. It may be supplemented by term or modified life insurance at the beginning of a partnership, but it is false economy to carry term insurance for any length of time.

PREMIUM PAYMENT

The payment of premiums should be made by the partnership itself. It should not be considered

a personal obligation on the part of the partners at all, except according to their several liabilities as members of the partnership.

BENEFICIARIES

A partnership should be the ultimate beneficiary under this form of policy. The original beneficiary appears as the "estate" of the partner, right and title being conveyed immediately by an absolute assignment to the partnership.

Under this form of settlement it should also be remembered that any insurance proceeds paid to the partnership at the death of a partner enhance the value of his share by just so much more. Each insured can agree on behalf of his estate to waive this right, and it is quite desirable to give this provision serious consideration.

ASSIGNMENTS

As mentioned in the preceding paragraph an absolute assignment must be made in favor of the partnership by the insured. This conveys all rights under a policy, including its cash value and proceeds to the partnership so long as that partnership may have an interest in the insured's life.

If it ceases to have an interest in his life the assignment may be released and the policy may become the property of the insured upon an equitable adjustment of cash values and other credits which should be bought from the partnership for a consideration.

AGREEMENTS

If the partnership wishes to have the proceeds under a policy of direct compensation used for some specific purpose it is advisable that such an understanding be put in writing in order that the survivors may be obligated to execute the disbursement originally agreed upon. It is unwise to enter lightly into any such agreement in a case where it might be more advisable to create a discretionary fund. Survivors should be left free to use their judgment except in those cases where all partners are agreed that some special use shall be made of the funds.

Any agreement so desired should be drawn by lawyers representing the partnership together with such assistance as may be rendered by the legal department of the insuring company and the underwriter in the case.

CASH VALUES

All cash values existing under policies absolutely assigned to the partnership are the property of that partnership. The cash values may be considered as assets of the partnership, and it may borrow upon them if temporary financing is necessary.

TAXATION

Premiums paid upon policies of this type are not a deductible expense of the partnership in making Federal income tax returns because the members of the partnership are the direct beneficiaries of the policy at the death of a deceased partner.

If the premiums on a policy are paid entirely out of the funds of the other partners, the insured in no way contributing to the premiums, no Federal estate or State inheritance taxes would be levied on the proceeds when paid at the death of the insured. This rule would not hold good, however, if the insured's estate benefits from the payment of the proceeds or if he has contributed toward the premium payments.

Example

Several years ago a partnership had been convinced that life insurance would provide the most satisfactory medium for liquidating the share of a deceased partner. At the time the original life insurance was written there were three partners operating as book publishers. Approximately three years after the life insurance plan had been accepted the senior member of the partnership died and the proceeds of his policy were immediately used by the survivors to liquidate his interest, and at the same time those survivors decided to carry on the business alone without admitting any new members. A year ago a life insurance underwriter made an intelligent analysis of their situation and discovered that whereas the amount of insurance then carried was adequate for the liquidation of each partner's interest, one grave discrepancy had been overlooked. Neither partner had realized to what extent the other was operating as a specialist, and this fact was very obvious to an outsider because the senior of the two, then a man of fifty-two, had complete supervision over the printing plant and the production problems of the company. The junior member, then forty-seven, was in reality the editorial staff and sales organization

combined. Consequently, they were each made to see that the survivor in the event of a death would be confronted by a gaping vacancy in his organization. It was suggested by the underwriter that life insurance be carried along the same general lines as their existing agreement, but with the subordinate understanding that all policy proceeds in excess of the amount necessary to execute a liquidation of the deceased partner's share should be used as a discretionary fund in order to compensate them for the loss suffered. Incidentally, the entire amount of protection was increased at this time from $50,000 to $125,000 on each life. An interesting sidelight in this case is the fact that both partners, realizing the serious situation in which they might find themselves, have started to give intensive training to two young men whom they feel will eventually be able to step into their shoes. Undoubtedly this will mean the widening of all insurance plans at some future date to include these two new men.

PROPRIETORSHIPS

CHAPTER XI

PROPRIETORSHIPS AND LIFE INSURANCE

This designation applies to all business organizations, large or small, which are not operating under a corporation charter or a partnership agreement. (See definition on page 16.) Here is a wide field of business activity varying from large mercantile and industrial organizations down to a one-man business like the corner butcher shop or drugstore. It also includes that very large group of professional or semi-professional economic units such as doctors, lawyers, teachers, authors, artists, actors, musicians, accountants, and insurance underwriters. In fact, anyone who dispenses knowledge for gain, in contrast to the person who sells a commodity.

Each one of these business activities constitutes a separate proprietorship, and as such provides a wide and substantial field for the application of life insurance as protection for the best interests of the proprietors.

One of the chief problems existing within most proprietorships is the successful perpetuation of the business in its original form when the man responsible for its development dies. It is very plain that a large and well-established business dealing in merchandise can be handed on to successors in a more tangible and concrete form than the clientele of a professional man who is considered to be at the other extreme of the scale. The professional man or the business man who is selling knowledge or service will have a very difficult task to control the activities of his clientele or list of customers in the event of his death. He will also be faced with the other problems contingent upon business settlement in the event of his death. With it all he will present a more vital need for business life insurance than any other form of business organization.

It is natural that a consistent economic policy should govern the activities of every business organization. No man is operating on a sound economic basis if he spends the greater part of his lifetime developing a business as a monument to his efforts, only to let it crumble when he dies.

Business life insurance cannot replace the sentimental association of a man to a business, but it can go a long way toward financial rehabilitation

of any proprietorship in the event of loss by death of the responsible human being. In other words, it insures the life of the business insofar as perpetuation is possible with the guiding genius gone.

CHAPTER XII

CREDIT REINFORCEMENT AND LIQUIDATION FUND

The proprietorship, according to a strict interpretation of the preceding definitions, is in reality a man, so that it is quite accurate to say that when such a man dies so does the proprietorship. This should bring the thought of business life insurance very close to the heart of any proprietor, because in the event of his death there is the immediate consideration of liquidation, as well as the reinforcement of the credit situation.

These two items have been discussed separately under "Corporations" and "Partnerships," but, owing to the fact that a proprietorship dies with its man, liquidation and credit reinforcement are virtually synonymous, and they are discussed simultaneously here.

It is very true and very possible that a man may provide a "business will," instrument of trust or agreement, which will declare his wishes as to the perpetuation of his business. The doctor may

name his successor, the owner of a big store may name the beneficiary of his business property, but the liquidation cannot be accomplished until the creditors have had satisfaction. Just as soon as their claims have been met, however, there is the instant problem of succession.

Here is a business unit which should not be allowed to disintegrate, but for which some provision should have been made to liquidate it favorably and profitably on behalf of the personal beneficiaries of the proprietor's estate. Shall the business go to a faithful employee? Shall the business go on the open market? Shall the business be operated by the estate, or shall it be allowed to disappear, showing no profit and leaving no reminder of its previous success?

It is understood that the professional man must carry his inherent ability with him when he dies. He cannot transmit it nor sell it in any way, except in the case of royalties or other such tangible rights which it may yield. He can, however, compensate for the loss of earning power in such a way that his years of training and experience may produce a guaranteed income to his personal beneficiaries.

The professional man should consider his daily activities as a bread-winner wholly on the basis of

business earnings, and if he seeks to liquidate his estate so that it will show assets in excess of liabilities he must provide for perpetuation of that income.

A proprietor's creditors will have a direct lien, but not necessarily a preferred claim, on life insurance proceeds on policies made payable to his estate; and it is only just and equitable that they should. The obligations are there and they must be met. If the deceased has not made provision for their liquidation prior to his death his estate will be saddled with them just the same. It is much better for the person incurring the obligations to arrange for their settlement rather than to make somebody unfamiliar with the circumstances labor over that very undesirable task.

It is a well-known fact that there are not many large proprietorships today, owing to the hazards of unlimited liability. For this reason, if for no other, such proprietorships as do remain in existence should see to it that all liabilites will be fairly and completely liquidated in the event of their death. They should further take very definite steps to provide for the liquidation of their business if its succession has not been provided for, so that the business will fall into the hands of a capable manager or group of managers.

CREDIT REINFORCEMENT

There is a separate classification which would involve the purchase of a business by successors from the proceeds of policies carried on the life of the proprietor. This procedure will be described under a new classification which will be discussed later on.

The chief concern at this point is for the liquidation of a business and the provision for the reinforcement of such interests as creditors have in the continued existence of the insured. Insurance carried by the proprietor and payable to his estate will be available to the creditors as well as for the use of those who will liquidate the business.

AMOUNT OF PROTECTION

One part of the protection must be for the amount of liability incurred by the proprietor and outstanding against him at any average period during the fiscal year. This might even be made large enough to provide funds for the maximum amount of outstanding liabilities against that proprietor at any time. In this latter way all creditors would certainly be compensated, so that the second consideration, that of liquidation, could be accomplished without obstruction.

Of course, a proprietor should carry life insur-

ance payable to his estate adequate to liquidate it in its entirety in behalf of a chosen successor. This would mean that an owner would provide the purchase price for his own business. Its succession in this instance would be in the form of a gift which would not deprive the estate of its worth in cash. For instance, if a proprietorship was estimated as worth $100,000 its owner reckons that his estate should have $100,000 for it, and in addition, that owner wants a faithful employee to have the proprietorship at his death. Hence, he should carry $100,000 over and above the amount he will need for meeting the demands of creditors. Otherwise the liquidating factor will involve protection against the possibility of loss which is virtually inevitable if the estate of the proprietor sells the business. No purchaser will pay the same price for a proprietorship with that man dead as he will with its creator living. The difference in these values is invariably referred to as "good will." Any proprietorship carrying an item of good will should realize that that item constitutes the amount of protection necessary to insure against loss in the event of a forced or even deliberate sale. Consequently, the amount of protection should equal the outstanding obligations on an average

basis or on a maximum basis plus the amount of the good will item.

In the case of the professional man the amount of protection includes the amortization of his liabilities, plus an amount which will provide an income as near to the one which he has been withdrawing as it is possible for him to carry. This latter item may be modified to such an extent that it will eliminate such part of the earned income as the insured has taken for his own existence, as well as taking into consideration the income from royalties and other rights which will continue after his death. Thus, the formula might be applied so that this amount for a liquidation fund would be equivalent to a principal sum which will provide sixty per cent of the insured's present income. A doctor earns $15,000 a year, gross. His business needs $5,000 of that amount, and he has provided $10,000 for himself and his dependents. This would mean that, on a five per cent basis, he would need to carry $120,000 life insurance to yield $6,000 or sixty per cent of his personal income. Add to this the amount necessary to meet whatever outstanding obligations may exist at the time of his death.

It is very true that the same formula may be ap-

plied to the mercantile or industrial proprietor. But in addition to the professional man who has been deriving an income from invested capital as well as from invested brains these two factors must be taken into consideration in determining the amount of protection necessary for liquidation on a favorable basis. All the proprietor needs to determine is "What is my business worth today, and what will it be worth tomorrow if I die?" This will not prove to be so difficult of solution as might be seemed at first glance. The prospective insured and the life insurance underwriter should be able to determine some fair amount capable of providing the execution of the former's wishes in the event of death.

POLICY FORM

Ordinary life insurance will constitute the best medium for providing the desired proceeds. Of course, a limited payment life policy may be applied if the earning power of the firm is to be greater over a subsequent period of years than it will be later on. It is recommended, however, that the case be reviewed in detail before limited payment life is used as the cases are few and far be-

tween where that form would be more desirable than ordinary life.

Term or modified life insurance may be used, but only with the understanding that it provides the desired amount of protection at the lower premium rate for the period with conversion anticipated just as soon as it is possible to do so. If credit is being reinforced either of these forms might be considered as more desirable, and this is one instance of their justifiable application.

Endowment insurance may be used if a retirement fund is desired. However, this procedure is not usually advantageous because the amount of endowment insurance would have to equal the amount of protection prescribed in the preceding paragraph. If the proprietor were to die before the maturity of the insurance as an endowment the protection must be equal to other needs. It may readily be seen that the amount of protection would not have to be so much if it were certain that the insured were to be alive when the endowment matured, because it then would be possible for the firm to liquidate its obligations deliberately and the highest price could be obtained in the event of a sale. Furthermore, endowment insurance may be used to amortize any obligation at

the end of a definite period of time. In other words, a man may have a credit of $10,000 for a fifteen year period matched by a fifteen year endowment policy on his life for the same amount. He thus insures the ultimate retirement of that obligation whether he lives or dies.

PREMIUM PAYMENT

Premiums on policies to meet this need are paid by the proprietor. This might very well be characterized as personal insurance because the premium payer and the insured are synonymous. However, if the proprietor keeps separate personal accounts and business accounts the premium payment should be made out of the latter.

BENEFICIARIES

Invariably it is best to name the estate of the proprietor as the beneficiary. Many proprietors might be inclined to name their personal beneficiaries in the policies. It should be noticed, however, that this is not the same as the procedure just outlined because the funds involved are thus placed beyond the immediate reach of creditors. In addition, the responsibility for the execution of liquidation falls upon the shoulders of the per-

sonal beneficiaries who are many times incompetent to perform the task required.

The policies of life insurance taken out by the professional man should be made payable to his "estate" so that such part of the amount of protection as should apply against outstanding obligations will be available. This recommendation is based upon the same theory as that just stated. The executors or administrators of the estate should be assigned the responsibility of adjusting the affairs of the insured because they possess sufficient knowledge of circumstances. However, such protection as will exist over and above the demand of creditors should be made payable directly to a personal beneficiary inasmuch as there will be no business to be sold. It is a very remote consideration to believe that the clientele of a doctor or lawyer can be transferred for value received. Consequently, this reverts to the previous statement that the beneficiary should be the personal beneficiary of the insured except for that amount of insurance which will be necessary to liquidate liabilities.

It might often be advisable to nominate a trustee who will be charged with the complete responsibility of distributing the life insurance proceeds. If and when this is done the trustee should be

named as beneficiary together with a statement of his or her authority to act as such.

There may be some variation necessary in the nomination of beneficiaries if an assignment is to be used at any time. Refer to the next paragraph for information as to when and where the beneficiary may be different when an assignment form is used.

ASSIGNMENTS

Either an absolute or collateral assignment may be necessary. The most frequent use of an assignment would come with the necessity of protecting creditors. The collateral assignment should be used when the assignee's interest may be variable; the absolute assignment when the assignee's interest is always equal to the full amount of the policy. Most insurance companies will require that the beneficiary of a policy under assignment shall appear as the estate of the insured. The policy is thus made flexible so that it can be varied without inconvenience or delay. If a personal beneficiary is used it would many times result in delay because additional signatures would have to be obtained. It is recommended that an assignment be used in every instance where it is the real intention of

the proprietor to protect completely the interests of a creditor who is entitled to full compensation immediately upon the death of the insured. This is the most efficient way of expediting a settlement.

The necessity for an assignment will be very infrequent when the insurance is to be used for liquidation purposes. If the funds are to be used for this form of settlement almost every desired result can be obtained by a proper use of the beneficiary clause in the policy itself. Consequently, it is wise to be sure that the beneficiary clause is inadequate before the life insurance underwriter suggests the use of an assignment.

AGREEMENTS

A proprietor should have a business will as a part of, or in addition to, his personal will. It should be in writing. It should not be a verbal understanding between two or three persons with the execution of the instructions left to chance and good faith. A business will should be the definite expression by the proprietor as to what shall become of his proprietorship in the event of his death. If a successor has been decided upon that successor should have his instructions in writing.

He should be appointed as such. The maker of this will should give at least as much thought to its composition as he does to the final distribution of his personal property. (See page 222.)

Such a will or settlement of liquidation procedure should be prepared by the proprietor's attorney, plus whatever suggestions or recommendations the life insurance underwriter can make in coöperation with the legal department of his own home office.

TRUSTS

Many times it will be desirable for a proprietor to create a trust agreement for the execution of succession in the event of his death. The instrument of trust should be an elementary and simple document whereby its creator designates what is to happen to the business. A trust company, for instance, can be named as the beneficiary in a policy under an instrument of trust which will explain the trust company's duties. These duties might include the transfer of such funds as may come due under life insurance policies, the operation of the business pending a final settlement, the actual selling out of the business if that is desirable, and the execution of any additional work

which may be requested by the maker of the will.

A trusteeship presents the distinct advantage of having an impersonal attitude maintained in regard to the final disposition of the insured's policy proceeds.

The trustee may also be responsible for the distribution of that part of the insured's protection which is intended to meet the demands of creditors. It might possibly be very awkward if a trust is in existence and no stated instructions have been incorporated into the instrument of trust in regard to the payment of creditors. Litigation may result and threaten the welfare of the entire plan. The efficiency of its execution will be impaired and the insured's business will suffer from the inevitable delay that will arise. It is, therefore, better to invest responsibility in the trustee for the execution of all transactions.

CASH VALUES

When a revocable beneficiary clause is in force the cash values are the property of the insured at all times. They are available to him for financing, and can be considered as quick assets of the proprietorship.

The existence of an assignment carries with

it to the assignee the right to the cash values. They are the sole property of the assignee under an absolute assignment, and they are the property of the assignee under a collateral assignment to such extent as that assignee's "interests may appear" in the value of the policy.

The dividends, if any, accruing on insurance of this form may well be allowed to accumulate with the idea of accelerating the maturity of the policy as this form of protection bears a marked similarity to personal life insurance.

TAXATION

Premiums paid on life insurance carried by a proprietor for purposes of liquidation or credit reinforcement cannot be considered as deductible business expense for Federal income tax purposes.

The proceeds of the policy paid as a claim at death need not be declared as income, however, unless there has been a transfer of the policy for a valuable consideration.

If the policy is payable to the insured's estate, the proceeds would have to be included in the gross estate when computing the amount subject to tax under the Federal estate and State inheritance tax laws. If the proceeds were payable to

named beneficiaries other than the estate, the same exemptions would be allowed under Federal and State laws as in the cases of personal insurance carried by the insured on his own life.

Example

There is a very interesting case of a theatrical producer who had originally been one member of a partnership. Personal incompatibility had caused distressing differences of opinion within that partnership, and about two years ago this man (who shall be known as A) withdrew to go into business for himself. A had marked ability as a playwright in addition to his training as a producer so he was well qualified to operate independently. He had been married and divorced, and a boy by that marriage had been placed in his custody. Money saved during his association with the partnership made it possible for him to operate alone although he did find it necessary to seek credit to support his productions. There were two problems which A wanted to have settled automatically at his death. First, he wished to be sure that, irrespective of the status of his productions, such creditors as might exist would not suffer a loss at his death. Second, he wanted to be sure

that his son would have a perpetual trust fund for his support. Consequently, at the suggestion of a life insurance underwriter, A took a policy of $250,000 ordinary life on his life payable to the Broadway Trust Company as trustee. This instrument of trust specifically stated that all commercial obligations outstanding against A's estate should be liquidated from this fund and that the remainder should be held in trust to yield an income to his son. Incidentally, this same instrument of trust included specific instructions regarding such royalty rights and producing returns as might accrue to A's estate. The trust company was directed to dispose of unproduced plays at a fair and reasonable price but it was not allowed to sell any plays at an unreasonable price irrespective of how long they were held. In other words, A's artistic temperament refused to consider the possibility of having cherished plays go on the auction block at a forced sale.

CHAPTER XIII

PURCHASE PLAN

Many proprietors have in their employ a man or group of men who have contributed largely to their success. Yet these men have never been participants in the profits except to such extent as the proprietor might care to enlarge salaries or distribute bonuses and commissions. These employees are usually of the type which have a very keen interest in the perpetuation of the proprietorship following its owner's death. They are even anxious in many instances to be the successors themselves and to operate that business as their own.

Furthermore, there is another large group of interested individuals which is made up of people indirectly affiliated with the proprietorship who are anxious to have its ownership revert to their possession in the event of the death of the proprietor. For instance, there is the interested party who has supplied support for the proprietorship in the form of guaranteed contracts for business et cet-

era. Such a party—an individual or a business—may not care to have the business fall into strange hands.

In any or all of these cases it should be distinctly understood that the proprietor is under no obligations whatsoever to the parties mentioned, and that he is not compelled to contract for the succession of his business except insofar as the arrangement may be agreeable to him. However, the proprietor may feel a moral responsibility to give a purchase option to his employees and associates or to his supporters, and for that reason he is willing to entertain the execution of the suggestion made in this chapter.

It is a known fact that there are many arrangements made for the transfer of a business on the basis recited here, but the execution has been arranged with long term notes or by the payment of the purchase price, as, if, and when acquired.

At this point life insurance may step into the breach as the most satisfactory known method of providing an expeditious execution of the transaction. The proceeds will have been acquired by virtue of premium payments which have been distributed over a period of years. The purchasers are able to buy the business by merely paying the interest on the money against the day when they will

need it. This condition is better than borrowing money because it may be necessary to use every cent of available capital for the actual running of the business. This is especially true if no liquidation fund of life insurance has been carried by the proprietor. It should be realized that no such purchase plan is possible in the case of the professional man. If a professional man dies, his clientele and his ability cannot be sold. Of course, his royalty rights or contract commissions and so forth can be sold by his survivors. Life insurance, however, would have no bearing on such a transaction.

In describing the methods for executing a purchase plan the word "purchaser" is used to describe that individual or that business which is to buy the proprietorship from the estate of the proprietor.

AMOUNT OF PROTECTION

This should be equivalent to the prearranged purchase price for the business. It may not be possible to determine an actual figure in advance, but the method of arriving at that price can be clearly established. The purchaser who will carry the insurance on the life of the proprietor should see to it that the amount of protection is always

as near that purchase price as possible. The efficiency of this entire purchase plan depends upon the existence of a satisfactory amount of life insurance to execute the sale. If the life insurance proceeds represent only one-quarter or one-third of the purchase price the purchaser is confronted with the problem of raising the balance.

During the lifetime of the proprietor he may set a satisfactory price on the proprietorship and the ultimate purchaser may agree to it under some form of written understanding which will be explained later. Furthermore, in the event of the proprietor's death the purchase price may be determined in a fair and equitable manner which will also be predetermined by mutual agreement between all interested parties. This also will be explained in the paragraph entitled "Agreements."

POLICY FORM

The ordinary life contract will be the most desirable and efficient in almost every instance of this type. It will provide the protection for the lowest net outlay, and for that reason should be of interest to all concerned.

The use of term or modified life insurance may precede the establishment of some permanent form,

but again it is recommended that it should not be considered as a substitute for the permanent forms.

Endowment insurance could be used to provide the purchase price of a proprietorship, but owing to the fact that the period of time must be known and that the premiums are proportionately high, it will seldom be used.

PREMIUM PAYMENT

Premiums will be paid in every instance by the beneficiary. If any other method of payment is contemplated the case immediately loses its identity as being of this section.

BENEFICIARIES

The beneficiaries should always appear as the estate of the proprietor subject to the immediate application of an absolute assignment which will he explained in the following paragraph entitled "Assignments."

It is also advisable to consider the appointment of a trustee for the execution of a purchase plan, in which case said trustee should be named as the beneficiary in the policy together with written evidence of such an appointment.

There may be other methods suggested by life insurance underwriters or by the proprietors involved, but in the last analysis it has been found that the method just stated provides the most complete satisfaction to those who are concerned with the efficient execution of the plan. The irrevocable beneficiary clause does not provide adequate protection for the rights of the premium payer, because the consent of the insured is necessary before any alteration is made in the policy. There is no reason for giving such consideration to the insured.

ASSIGNMENTS

In the paragraph entitled "Premium Payment" it was stated that the premium payer should be the beneficiary, and in the paragraph entitled "Beneficiaries" it was futher stated that the beneficiary should be the estate of the insured plus the immediate application of an absolute assignment. This is all brought to a conclusion by stating that the assignee under an absolute assignment should be the party or parties who have taken out the insurance on the life of the proprietor. An absolute assignment conveys to the purchasers all right, title, and interest under the policy. It affords the complete protection which they must

have, and yet at the same time it makes it possible for the policy to be released to the insured if for any reason the purchase plan is discontinued.

AGREEMENTS

The services of a lawyer should be engaged to draw up a contract which will explicitly state the purchasing power which is being conveyed by the proprietor to the purchaser. The document should be simple and direct, and its chief component part should be that section which describes the method of arriving at a fair purchase price when the proprietor dies. It is suggested that such items as the value of good will, inventory, accounts receivable, salability of product, existing markets, actual value of the insured's life as an asset should govern those who draft the agreement. It is quite customary, in cases of this kind, for each interested party to choose an appraiser. These appraisers will then be requested to add another appraiser of their own selection. Each party will protect its several interests, and for that reason the life insurance underwriter should not be called upon to do more than insist that some agreement shall accompany the life insurance policies.

The lawyer should naturally consult the life

insurance underwriter who in turn will consult his own legal department in any case involving the life insurance contract, because no agreement should attempt to bind the life insurance company beyond its powers as prescribed by law.

Example

THIS AGREEMENT, made this 28th day of March, 1927, by and between Richard Roe, party of the first part, hereinafter called the VENDOR, and John Doe, party of the second part, hereinafter called the PURCHASER, both of New York, WITNESSETH:

1. The said vendor agrees for himself, his executors and administrators to sell to the said purchaser and the said purchaser agrees to purchase of the vendor at the valuation and upon the terms hereinafter mentioned, the hardware store (now owned by the party of the first part) known as "The Steel Hardware Company" located at 551 Fiske Street, New York, New York, as a "going concern" including all the stock, implements, utensils in trade, fittings, fixtures, furnishings, effects, wares, merchandise, and articles of every name and nature whatsoever being now on the premises or used or designed to be used

in and about the premises including also the Good Will of the business and the use of the name of the party of the first part or such trade name, names, and labels as may be now used in the business, said sale to be made as soon after the death of the vendor as possible, in the manner hereafter outlined.

2. Within thirty days after the death of the vendor an appraisal shall be made of the said business—The Steel Hardware Company—in this manner. The said executors or administrators and the said purchaser shall each appoint an appraiser and the two so appointed shall choose a third and these three shall determine the price for which the business shall be sold and purchased. In the event of the neglect or refusal of either the said executors or administrators or the purchaser to name an appraiser or of the appraisers so named to determine the value of the business, within the said thirty days, the value determined by the appraiser named by the other party shall determine the sale and purchase price.

3. The purchaser hereby agrees to pay the purchase price determined as provided in paragraph 2 to the executors or administra-

tors of the vendor within thirty days after determining the purchase price as hereinabove provided and the said executors or administrators of the vendor shall deliver a good and sufficient bill of sale of the said business —The Steel Hardware Company—and shall deliver up the full and peaceable possession of the said store, premises and entire subject matter of this contract to the purchaser or his agent upon payment of the purchase price as herein determined, provided, however, that if the purchase price shall exceed $50,000 (the assumed face value of the life insurance policy carried by the purchaser upon the life of the vendor) such excess may be paid by note or notes of the purchaser, all of which notes shall fall due and payable within six months from date.

In witness whereof the parties hereunto set their hands and seals on the day first above written.

L. S. _____

L. S. _____

TRUSTS

It might be well to consider the advisability of appointing a trustee who will be responsible for

executing the sale of the business on behalf of the insured and the purchasers. This being the case the trustee will be appointed under an instrument of trust which will embody any agreement as outlined in the preceding paragraph. The trustee shall be charged with the responsibility of continuing the life insurance so long as he shall be provided with the necessary funds with which to pay premiums, so that in the event of the proprietor's death the trustee will be in a position to negotiate the sale on behalf of the seller and purchaser alike. The impersonality of a third party is very desirable, especially if a large amount of money is involved.

CASH VALUES

The cash values should always be the property of the purchaser. The absolute assignment provides this without question. It is only when some variation of this form of beneficiary clause is used that the purchasers must see to it that their rights to the cash values are protected. The insured (the proprietor) should have no access to these assets until such time as the insurance may revert to him for any reason.

TAXATION

The premiums do not constitute a deductible expense in the Federal income tax return of the premium payer, for under the plan outlined in the preceding paragraphs he would be directly or indirectly a beneficiary. It is quite obvious that the insured has no interest whatsoever in the policy, and so the premiums do not figure one way or the other in his income tax return.

If all premiums were paid by the beneficiary on a policy payable to the beneficiary, no Federal estate or State inheritance taxes would be levied on the proceeds at the death of the insured. However, if the proceeds were paid to the estate of the proprietor in exchange for his rights to the proprietorship such money would become a part of the proprietor's taxable funds in computing inheritance or estate taxes.

Example

By virtue of a splendid location, a discerning eye for public taste, and an inherent love of books a bookseller had "arrived." His first place of business had been no more than a stall whereas the present establishment represented all that was

modern in the display and marketing of current publications and rare editions. The bookseller had established an enviable name for himself, but he had gone serenely on his way without giving a thought to what would happen to his business. At the age of fifty-six he was approached on the subject of business life insurance. Not one spark of interest was revealed. "I am a widower without children and I have instructed my executors to sell such books at auction as cannot be returned to the publishers." The situation seemed really hopeless until it was learned that a competitor in the same city wanted very much to obtain the bookseller's establishment and stock. The two proprietors had always been friendly, and by means of a life insurance agreement the competitor obtained all rights to the bookseller's business at the time of the latter's death. The bookseller agreed on behalf of his estate to surrender lease, stock, and good will to the former. A clause in the agreement which they executed qualifies this transaction by specifying that the purchase price shall be determined by three appraisers—one chosen by the estate, one by the competitor, and the third by these two. Only the appraisal price is to be paid by the purchaser. If the appraisal price is in excess of $125,000 the estate of the bookseller is

to accept five equal annual payments plus five and one-half per cent interest. The figure of $125,000 was estimated as a fair worth of the business eighteen months ago, and the competitor took out an ordinary life policy on the bookseller for that same amount.

CHAPTER XIV

DIRECT COMPENSATION

The need for protecting the economic interest in the human assets of any proprietorship is as vital and as worthy of consideration as the same need in a corporation or a partnership. Whether it be an employee of particular training and ability, or whether it be a contracted party there is no reason why the proprietor should be called upon to suffer a financial loss if services being rendered by these men are stopped by a death.

The compensation takes the form of a fund which will provide a replacement purchase price because money may be most necessary in obtaining the services of some new man. Furthermore, such a fund will, in part, compensate the proprietor for the investment of both time and money which he has made in the deceased man's development; or, in the case of a contracted party an investment which the proprietor has made by virtue of that party's peculiar ability to execute the work ordered.

The need is far more predominant in commer-

cial or industrial proprietorships than it is in the case of the proprietorships which are composed of professional men and their activities. There may be scattered instances of a professional man who directly employs the services of an expert or valuable employee as well as establishing a contractual relation with an individual for the execution of some particular piece of work. In these cases the formulas prescribed will apply just as accurately as they are intended to do for the mercantile or industrial proprietorships.

In either instance the full force of the loss is brought home to the proprietor when it is necessary for him to assail his profits or capital in order to meet the loss which results when death removes a human asset. Furthermore, it seems to be a very peculiar fact that most proprietorships, being but a reflection of one man's activity, have overlooked the establishment of a method of development which will automatically replace, insofar as it is humanly possible to do so, the loss of a human asset from that proprietorship's own personnel. Proprietors go on building their businesses, totally oblivious of the fact that death will some day interrupt their activity and thus present to their successors the problem of replacing their leader's dynamic energy. Frequently men will re-

fer to such executive heads as being of the "old school." This refers to the executive who insists on retaining complete control of the operation of his proprietorship.

Naturally this would seem to involve a consideration of a compensating fund for the loss of the proprietor himself. This has been referred to, but perhaps not in the exact words, in the preceding section entitled "Credit Reinforcement and Liquidation Fund."

Much thought must be given to the fact that as these proprietorships expand and develop, a certain percentage of their personnel expands and develops with them. The loss of any one of these human assets by death always drives home the fact that in reality he has constituted an important cog in the machinery of that proprietorship's operation. It is by way of calling attention to these employees or associates that this condition has been explained in detail.

The methods to be used in providing protection for these needs are presented in the following paragraphs.

The Valued Employee or the Expert

Protection for the valued employee or the expert should be considered from a different angle

than in the case of a contracted party who is not an employee of the proprietor. The distinction should be quite clear because the valued employee or expert may be described as a man in the permanent employ of the proprietor. All of the employee's ability and services are at the disposal of his employer and the employee is not a proprietor as such, as might well be the case with a contracted party.

If a man is developed to the point where he is becoming a distinct asset to the proprietorship all salary paid prior to that time may be said to be a partial payment plan for purchasing his efficient productive power. Consequently, if, at the peak of his productivity, he dies, the real purpose of the investment has disappeared and a large part of the money paid in is lost. It is quite comparable to the instalment buying of an automobile which, as soon as it is paid for, is destroyed by fire. Insurance would be carried on the automobile, and for the same basic reason it should be carried on the man.

AMOUNT OF PROTECTION

One of the most workable formulas that can be applied in arriving at the amount of protection necessary is ten times the average annual salary

payment. Both the expert and the employee may possibly be responsible for the execution of some contract the profit from which may be reckoned in dollars and cents, and, in that instance, the amount of protection should be equivalent to their financial responsibility. The expert may have developed some vital attribute in the proprietorship's productive power, and the proprietor may even have invested capital against the expert's ability. Here again is another known amount which can be used as a gauge for the amount of protection because the amount of money at stake certainly gives some guide to the worth of the expert. In the case of the employee an additional consideration might be that the amount of protection should be equivalent to the employer's estimate of the actual price that must necessarily be paid to replace the employee in the event of the latter's death.

POLICY FORMS

The ordinary life contract should be the standard form for providing protection for these needs. The use of term insurance is emphatically discouraged in this case, whereas modified life insurance may be justified occasionally if a low initial premium is necessary.

PREMIUM PAYMENT

The proprietor receives the entire benefit of this protection so he should pay the premiums.

BENEFICIARIES

The beneficiary of these policies should always be the proprietor, and for that reason the standard form of application should be made out to him as the absolute beneficiary unless it seems desirable to use an assignment in order to further secure his interests as beneficiary. If an assignment is to be used the actual beneficiary nomination in the policy should originally be the estate of the insured, subject to immediate conveyance of the beneficial rights by the insured to the proprietor.

ASSIGNMENTS

An absolute assignment of the interests under these policies to the proprietor by the employee or expert upon whose life they have been placed will mean that entire right and title are vested in the proprietor. This is as it should be. It is consequently recommended that the beneficiary rights should be so protected, and the proprietor is thoroughly justified in requesting the execution of such an assignment by the insured. No part of

the assets or rights under these policies should be available to the insured so long as the proprietor maintains the policy. The life underwriter who applies the assignment is again cautioned to be sure that the assignment is removed as soon as the proprietor's insurable interest in the insured's life has ceased, thus giving the latter the opportunity of carrying the policies himself.

CASH VALUES

If the irrevocable beneficiary clause is used the cash values cannot be considered as clear assets of the proprietor. True, these cash values may belong to the proprietor but at the same time they cannot be released without the signature of the insured, and this is really a disadvantage to the proprietor. Thus it is contended that they are not the same quick assets that they would be if the beneficiary were protected by an absolute assignment in which case the cash values are accessible to the proprietor without reservation.

TAXATION

The premium payments could not be considered a deductible expense by the proprietor in making Federal income tax returns. Transfer taxes would

not be levied upon the proceeds of these policies at the death of the insured since, under the plan outlined, all premiums would be paid by the beneficiary and the proceeds would never become a part of the insured's estate. Of course, this statement would not hold true if the policy were reassigned in favor of the insured, the premium payments being made by him.

Example

An architect in a middle western city had spent the best years of his life after leaving college at his profession. He had specialized in commercial construction and had been successful to such an extent that his name on a piece of work was a "hall-mark" in the profession. However, at the age of forty-seven he suffered a nervous breakdown and was confined to his home for three months. During his enforced absence the work of the office was turned out by three assistants who had been trained in their work by the proprietor. Upon recovering from his breakdown the architect was ordered by his physician to travel for at least a year. Furthermore, he was forbidden to return to his office except in a supervisory capacity. Long before the breakdown the architect had

listened to the suggestions of life underwriters without reacting favorably but the misfortune itself spoke volumes and in unmistakable terms. Before leaving on his trip each assistant was covered by ordinary life insurance for $50,000, each policy naming the proprietor as beneficiary, inasmuch as the death of any one of these assistants might impede or even suspend work on a commission indefinitely, with its resultant loss to the proprietor.

Contracted Parties

A proprietor may enter into contract with an individual or group of individuals to execute a commission. The satisfactory completion of this work depends upon the continued existence of one or more men. The death of any of these men would impair the work to such an extent that there would be a loss of money. Life insurance again is recommended as the medium to be used in providing the compensating factor in the event of such a loss. A proprietor negotiates to have work done, but he has no control whatsoever over the hazard of death, and for that reason can only prepare himself as best he may to continue work under other supervision if it is necessary. This procedure may

necessitate the abandonment of the initial plans, or the newly contracted party may prove to be less efficient than his predecessor, all involving added expense to the proprietor. The use of life insurance means that the responsibility for the financial burden is shifted by the proprietor to the life insurance company, upon payment of the premium.

AMOUNT OF PROTECTION

If the death of the person or persons under contract would result in a total loss of the project undertaken, naturally the amount of insurance should equal the cost of the project. With this as a maximum, a lesser figure may be arrived at on the basis of proportionate loss resulting at the time of the contracted party's death. In addition to this, it is desirable to discount the recovery value of the work already done because a successor might be able to reclaim a reasonable proportion of the work. This being so, the proprietor entering into contractual relations with another party should determine for himself what possibility there is of replacing the ability which they have under contract. There must be some amount of insurable interest because it is assumed that the proprietor

has under contract the most desirable party obtainable, and any replacement must at least be second best, leaving a margin between the efficiency and worth of the first party and the second party. The attention of life underwriters, as well as proprietors contemplating this form of protection, is called to the fact that life insurance companies must necessarily eliminate any element of speculation involved in placing this kind of protection.

POLICY FORM

Ordinary life is the best policy form to be used. However, term or modified life insurance may be justifiably applied in certain instances. Such circumstances are fairly obvious because the period of insurable interest may be very short, and will undoubtedly come to an abrupt end when the contract is fulfilled. Hence, a one to five year term policy may be used, but in no circumstances is it recommended that term insurance be taken for a longer period, inasmuch as ordinary life will invariably show a lower net cost. A modified life contract would be very much better than term insurance especially if the original need for protection were to disappear and the insured had expressed

a definite desire to continue the protection for himself.

PREMIUM PAYMENT

Premiums should be paid by the proprietor unless there is some explicit understanding with the contracted party that the latter should carry the insurance and hence pay the premiums.

BENEFICIARIES

In any case the proprietor should be named as the absolute or irrevocable beneficiary. If, however, he pays the premiums, the right and title under the policy should be conveyed to him by the contracted party, in which case the insured first names his estate as beneficiary and then executes an absolute assignment of the policy to the proprietor. On the other hand, if the contracted party is paying the premium, the proprietor has no absolute right to the cash values under the policy, and for that reason an absolute or irrevocable beneficiary clause is sufficient.

ASSIGNMENTS

It has been stated previously that an absolute assignment is often used in transferring right and

title in a policy of this type, but this should be supplemented by saying that a collateral assignment is sufficient if the interests of the proprietor are, for any reason, to be restricted to an amount equal only to his interest in the policy and the policyholder.

CASH VALUES

If the proprietor owns this form of protection by virtue of an absolute assignment, then the cash values may be declared as his assets, for these cash values are at all times available to that proprietor irrespective of the wishes of the insured. However, where the policy is issued with an absolute or irrevocable beneficiary the cash values presumably belong to the beneficiary, but they cannot be disturbed or withdrawn except with the consent of the insured, thus establishing them as assets in escrow.

TAXATION

If the proprietor pays the premiums and is the beneficiary the premiums cannot be deducted as expense when filing an income tax return. If, on the other hand, the contracted party pays the premiums and the proprietor is the beneficiary, the tax authorities might, under some circumstances,

allow the insured to deduct the premiums an as expense, but this deduction should be made only on the advice of his lawyer or of a person familiar with tax rulings and the particular situation which exists.

If the proprietor, as beneficiary, pays all the premiums on the policy, inheritance and estate taxes would not be levied on the proceeds at the death of the insured because the proceeds do not become a part of the insured's estate. This statement might not hold true, however, if the insured pays the premiums. Nor would it hold true if there were any change made in the policy when the contractual relationship ceased to exist and the policy was returned to the insured.

Example

A concert and entertainment manager had contracted with a foreign operatic star for fifty concerts to be given in the United States over a period of two years. The manager calculated his gross profit at approximately $50,000. Although the death of the star during the contract period would not necessarily mean a total loss of income to the manager, he nevertheless refused to support any part of the hazard himself. He insured

his source of income for $50,000 on a five year term contract and, in addition, he was instrumental in adding a substantial volume of life insurance to the personal estate of a young lady who had hitherto been ignorant of its worth.

GENERAL CONCLUSION

CHAPTER XV

COÖPERATION

One of the most valuable contributions to the success of any case of business life insurance is coöperation between the life insurance underwriter and the prospective client.

This statement naturally presupposes the fact that the underwriter is an individual who has made a comprehensive study of the entire subject of business life insurance and that he has successfully placed himself in the confidence of his client. Such a result will have to be obtained by virtue of service rendered to other clients, and by virtue of that assurance which is bound to come to the underwriter as the result of his own confidence in his knowledge of the subject.

The client, on the other hand, should be made to understand that only by complete coöperation with the underwriter will it be possible for the best work to be done. Inadequate protection, improper underwriting, and absolutely incorrect provisions are only some of the distressing results

of a restrained and uncoöperative attitude on the part of the client.

If the client requests information of the underwriter which the latter knows he is unable to answer from his own fund of knowledge, he should refrain from venturing a guess or supposition. This is true in discussing business life insurance to a greater degree than in the case of personal life insurance, because it is invariably far more difficult to set an error right in the former instance than in the latter. It is a temptation to respond glibly to any request which may be made by the client, and for that very reason it is the duty of the underwriter to proceed just as slowly as a lawyer would do under similar circumstances. The lawyer always refuses to place himself on record unless he has first had the opportunity to verify his commitments. The underwriter should school himself to do likewise.

However, if every client would place before the underwriter all of the facts and information which pertain directly, or even indirectly, to the case at hand he will receive a far more effective plan. He will also find that the test of experience will substantiate the prudence and acumen of the coöperation which he has extended to the underwriter.

The Questionnaire

In this connection and with the idea of offering some common ground upon which all interested parties may meet at the inception of a business life insurance case, a questionnaire has been compiled and offered which outlines the salient points upon which an underwriter should base his recommendations and his case. It is obvious that the questionnaire is extremely comprehensive, and in that connection it should be remembered that only occasionally will the underwriter be able to procure the answers to all of the questions. The data requested have been grouped according to the method of doing business, and the underwriter should immediately determine the form of his client's business organization, and then proceed to the completion of that portion of the questionnaire. The client may demonstrate his willingness to coöperate by answering just as many of the questions as he can, provided, of course, that no real confidences are violated by his doing so. Then, with that information, the underwriter should prepare a conservative yet comprehensive plan of protection. He should further be able to substantiate every single move which has been or will be recommended.

Business Life Insurance Questionnaire

Name of Business Organization .....
Address .....
Name of Person Interviewed .....
Is it a Corporation? ..... Partnership? ..... Proprietorship? .....

CORPORATIONS

How many stockholders are there? .....
What is the total authorized capitalization? .....
How much paid in preferred, if any? .....
How much paid in common .....
Number of shares of each, (pref.) .....
(common) .....
Is there any obligation in the stock certificate stating that it must be offered to the corporation first when it is put on sale by its present owner? .....
How few can control? .....
Who are they and what are their positions? .....
How much stock does each individual hold? .....
How many stockholders might be interested in a stock liquidation plan using life insurance? .....

What are their birthdays? . . . . . .
Are they in good health? . . . . . .
Are they married? . . . . . .
Have they made personal wills? . . . . . .
What stockholding executives are active factors in the management of the business? . . . . . .

. . . . . .

What are their birthdays? . . . . . .

. . . . . .

Are they in good health? . . . . . .
Who are the endorsers of the corporation's liabilities? . . . . . .
What are their birthdays? . . . . . .

. . . . . .

Are they in good health? . . . . . .
Who are the principal creditors? . . . . . .

. . . . . .

What is the average annual liability on the basis of a five year record? . . . . . .
What men *in the employ* of the corporation are valuable? . . . . . .
Why? . . . . . .
Is it possible to have a statement of earnings which will be kept absolutely confidential? . . . . . .
What life insurance, if any, is now carried by the corporation or by stockholders for direct or

indirect benefit of the corporation? .....

.....

PARTNERSHIPS

General? ..... Limited? ..... Trading? ..... Non-Trading? .....

Are shares equal? .....

If not, what is the distribution? .....

.....

What partners are married? .....

What are the birthdays of the partners? .....

.....

Are they in good health? .....

What partners have made a will? .....

Who are the endorsers of the partnership's liabilities? .....

.....

What is the average annual liability on the basis of a five year record? .....

Who are the principal creditors? .....

.....

What men *in the employ* of the partnership should be insured? .....

.....

What are their positions? .....

What are their birthdays? .....

Are they in good health? .....
What life insurance now carried can be considered as relating to the partnership? .....

.....

Is it possible to have two confidential figures?
First, What is the partnership worth today?

.....

Second, What were its earnings last year? ...

.....

Is it possible to see your partnership agreement?

.....

PROPRIETORSHIPS

Who is the Proprietor? .....
Married or single? .....
Any children likely to acquire the business?

.....

Is the Proprietorship trading or non-trading? ..

.....

Has the Proprietor made a will? .....
If so, what disposition has been made of the Proprietorship, if any? .....

.....

What life insurance is now carried by the Proprietor? .....
Who are the beneficiaries? .....

Who might be interested in buying the assets of the Proprietorship after the Proprietor has died? . . . . . .

. . . . . .

What is the basis of their interest? . . . . . .

What are the assets and inventory worth today?

. . . . . .

What do they yield per annum? . . . . . .

Physical and Medical Service

Many cases of business life insurance involve several men. Possibly all these men are not to be insured, but there are at least others who will be called upon to give time and consideration to any insurance plan which may be contemplated by their company. For this reason it is advisable to establish all questions of insurability at a very early stage in the procedure. No underwriter should knowingly consume the time of his clients with a discussion of the desirability of an insurance plan unless it is a known fact that the applicant or applicants for insurance will pass the medical examination. This condition can be determined just as soon as the clients have been convinced of the justifiability of coöperating with the underwriter.

It is quite conceivable that there will be re-

peated instances of uninsurability among applicants for business life insurance. If and when such a problem arises it will undoubtedly have to be met by an intelligent manipulation of all plans of protection so that the excluded risk will be able to participate on some other basis. No attempt has been made to provide a panacea for this difficulty. Each case must be handled as it arises and each case must be handled in terms of the specific problem presented. By way of example, a far-fetched possibility may be cited. Two partners, wishing to provide an insurance fund for the liquidation of their business, decided to submit to physical examinations early in their investigation, and much to the surprise of both it was discovered that B was uninsurable. They were about of an age, A being 47 and B being 45. The underwriter recommended that A carry $50,000 ordinary life insurance, and this was duly executed. In addition, it was decided that they would carry $50,000 twenty year endowment on A's life, but with B appearing as the absolute beneficiary by assignment. However, it was expressly stated in writing that if A died first all proceeds of the twenty year endowment policy would accrue to A's estate, irrespective of the proceeds of the ordinary life policy which would be used, according to the

agreement, by B in settling with A's estate for his share in the partnership. If B were to die first, but before the twenty year endowment had matured, all values existing on that policy would be payable to A and he in turn would use that money toward buying B's interest. Then again, if the endowment matured prior to B's death but B did die before A, the latter would thus have the full purchase price of B's interest because the agreement had been compiled to provide for that contingency.

That is a very involved example of the extremes to which clients may be willing to go in order that they may insure the proper functioning of an insurance plan. It is not considered good business for an underwriter to force the execution of such a plan except when he has the complete confidence and coöperation of all concerned.

In general, it may be said that a business should take steps to protect itself in any way possible against the inevitable loss of any human asset who is discovered to be uninsurable. Of course, mortality tables are only actuarial averages, but even so, they are the best guide and in spite of the exceptions they should be recognized. The same is absolutely true of any underwriting point of view which may be held by one or several life insurance

companies. An underwriter should make every effort to obtain insurance for his client even though it be on a sub-standard basis.

Furthermore, it cannot be emphasized too strongly that every man in a business organization, who is now or who may be at a later date a part of an insurance plan, should submit himself regularly and periodically for some sort of an authorized physical examination. Any corporation, partnership or proprietorship has the right to know the exact physical condition of its vital human assets. There may be a natural, yet unjustifiable reluctance to know the truth, but the facts should be known, even if the examinations are at the expense of the client or the underwriter himself.

Sub-standard Rating

The intricacies of determining the correct sub-standard rating cannot be discussed here, as it would involve an understanding of many underwriting, medical, and actuarial problems, and no underwriter in the field can be expected to master them.

However, it should be realized that a policy is rated on a sub-standard basis in order that the insured may obtain protection at an added rate

which has been figured as fair and equitable in view of his impairment as compared with tables of experience which have been accumulated from similar disorders. A client who is unable to obtain standard insurance but who is able to obtain substandard insurance has benefited by the progressive development of underwriting practice. Sometimes the insured is reluctant to accept such a policy, and it is the duty of the underwriter to explain very carefully and most comprehensively, if necessary, just how the insuring company has arrived at its conclusion.

By way of comparison, suppose that a standard fire risk were defined as a concrete and steel building equipped throughout with regulation sprinkler system, alarms, and fire windows and doors, located one block from a modern fire station and readily accessible to two high-pressure hydrants. With this as a standard any business man would readily concede that a frame dwelling located five miles out in the country and one-half mile from the nearest village cannot be considered, in comparison, as a standard fire risk, especially if it is not equipped with any fire-fighting apparatus. The rate for such a risk would be much higher than for a risk such as the one cited as being "standard."

The situation in life insurance is more or less identical. A standard risk receives a standard rating. The individual who presents the greater hazards of short life should be asked to realize that his lowered expectancy must be compensated by a higher rate. As a matter of fact he is really fortunate—as is often true in fire insurance—to find a company which is willing to insure him at any price.

Of course, an underwriter should obtain standard protection for his clients in every case when it is possible. Failing to do that, the client should evidence his confidence in his underwriter and the plan which has been approved to the extent of accepting sub-standard insurance if it is necessary to do so.

Total Disability and Double Indemnity

It is taken for granted that, even if a client or an underwriter is unfamiliar with these two clauses, it is possible to obtain a detailed description of them from other sources.

Neither total disability nor double indemnity has been discussed in previous chapters because they are not generally available, and because it is not customary for an underwriter to recommend the placing of insurance in a business life insur-

ance case so that the clauses might or might not be obtained. Frankly, the opinions as to the desirability of their use as a form of business protection are so conflicting at the present time that any intelligent analysis of their benefits would be virtually impossible. However, that does not mean that their use should be discouraged. Quite the contrary, if any underwriter is able to provide them for a client who is interested, it should be done and done as efficiently as possible.

Conclusion

Finally, the best evidence of coöperation which an underwriter can give to his clients is an active and constructive interest in their insurance plans *after* they have been put in force.

Once a year any business organization audits its books and endeavors to establish its financial standing. Therefore, once a year every underwriter should provide a statement for each client showing the financial standing of his life insurance. In addition, all elements of the case should be reviewed.

1. Are the amounts adequate and correct?

2. Is the form of policy still the best which the insured can have?

3. Are the premium payments being made according to the best interests of all concerned?

4. Should the beneficiary nominations be changed?

5. Are there any obsolete assignments outstanding?

6. Have there been any changes in the income or inheritance tax laws which would vitally affect anybody interested directly or indirectly in the insurance?

Lastly, the attorney for the corporation, partnership or proprietorship should be asked to review all outstanding agreements. Changes may have taken place in the financial status of the company. Interests may have been bought up or extended. Promotions or demotions may have materially changed the original insurance plan. Any one of several other fundamental variations may have been effected. Therefore, once a year the lawyers for the business should be consulted in company with the managing executives or any other principals in a business life insurance plan. By such coöperation the underwriter and the client may be as sure as possible that each and every case has been brought up-to-date, and that there will be that much better execution of all of the plan's protective functions when it matures.

INDEX

INDEX

accountants, 195
actors, 195
agreements, 35-6, 62-3, 84, 95-7, 124, 137, 141, 154, 158, 189, 198, 209-10, 218, 221-2; examples of, 98-113, 154-8, 222-4; warning concerning, 35
amortization of liabilities, 60, 203
artists, 195
assignee, 46, 176, 212
assignments, 33, 40, 63, 71, 76, 94-5, 140-1 153-4, 188, 211, 219, 220-1, 234; absolute —, 33, 62, 63, 140-1, 176, 181, 208, 220, 235, 240; collateral —, 33, 62, 63, 76, 77, 94, 141, 177, 182, 208, 241; obsolete —, 261
attorney, 85, 93, 96, 160, 166
authorities, tax, 42, 77, 78, 86, 142, 143
authors, 195

beneficiaries, 31, 37, 61, 75, 84, 88, 92, 140, 152-3, 166, 176, 181, 188, 206-7, 219-20, 234, 240; wives as, 93
beneficiary, 10, 31, 40, 53, 70, 71, 74, 76, 93, 124, 125, 140, 152, 176, 199, 206, 219, 226, 234, 235; absolute —, 152, 153, 177, 181, 207, 208, 234, 240; "estate" named as —, 176, 188, 207; irrevocable —, 152, 153, 177, 220, 240; "secondary" — clauses, 33; "special" — clauses, 33; wife as —, 31
Business Law (quoted), 49, 133-4
business will, 36, 95-6, 98, 188

cash values, 39, 40, 63-4, 71, 77, 85, 124, 141-2, 151, 177, 182, 190, 211, 225, 235, 241
coöperation, between life underwriter and client, 27, 247-261; between underwriter and company's legal department, 154, 189, 222
contracted party, 21, 73, 76, 179, 182, 232, 237-243
Conyngton (quoted), 49, 133-4
corporations, 17, 18, 25, 50, 172, 198, definition of, 49-50; direct compensation for loss of officers, 22, 80-1; — and business life insurance, 50-54; life insurance as credit reinforcement for, 55-66; legal rights of, 54; direct compensation for loss of valued employee and expert, 67-8
Court of Appeals of New York, 86

creditors, 140, 201, 211, rights of against partnerships, 137
credit reinforcement, 17, 18; for corporations, 55-66; for partnerships, 136-146, 173; for proprietorships, 198-214

direct compensation, 19, 137, 138; for loss of valued employee or expert, 20, 67-8, 174-5, 231-232; for loss of contracted parties, 21, 176, 233; for loss of officers of a corporation, 22; for loss of members of a partnership, 22, 185-6; for corporations, 67-87; for partnerships, 172-92; for proprietorships, 229-243
disability, total, 259-60
dividends, 43, 45-6, 212; stock, 97
doctors, 195

employee, the valued, 20, 67-8, 174-5, 231-2
endowment policy, 30, 64, 91, 149, 205, 218
estate tax, 41-45, 64, 71, 78, 85, 125, 126, 143, 167, 177, 183, 190, 212, 226, 241, 261
examples, of credit reinforcement, 65-6, 144-6, 213-214; of direct compensation, 72-3, 78-80, 86-7, 178-9, 184, 192-3; of liquidation funds, 98-113, 114-124, 126-129, 161-6, 168-71, 213-4, 236-7, 242-3; of purchase plan, 226-8

Federal income tax, 41-5, 64, 71, 77, 85, 125, 142-3, 167, 177, 183, 190, 212, 226, 235, 241, 261
fire insurance, 56

good will, 202, 203; importance of properly estimating, 28

human asset, 55, 227, 230
human value, 56

indemnity, double, 259–60
institution, fiduciary as trustee, 160
instrument of trust, 32, 198
insurable interest, 73, 176

lawyer, 52, 189, 195, 221, 248
legal rights of corporation, 54; of creditors against partnership, 137
life insurance, 7, 13; need of in business, 14; origin of, 7; — and business, 11; classification of, 15; uses of, 18-23; ordinary —, 28, 30, 69, 75, 83, 91, 139, 149, 175, 180, 187, 204, 218, 233, 239; limited payment, 28, 30, 83, 91, 139, 204; endowment, 28, 30, 64, 91, 149, 205, 218; term, 28, 30, 61, 75, 149, 180, 187, 205, 218, 233, 239; modified, 28, 39, 61, 75, 149, 180, 187, 205, 218, 239; as "shock absorber," 82
limited payment life insurance, 28, 30, 83, 91, 139, 204
liquidation fund, 23, 137, 160; corporation, 23, 88-129; partnership, 23, 147-171;

proprietorship, 23, 198-214

minimum price clause, 96
modified life insurance, 28, 30, 61, 75, 149, 180, 187, 205, 218, 239
musicians, 195

ordinary life insurance, 28, 30, 69, 75, 83, 91, 139, 149, 175, 180, 187, 204, 218, 233, 239
"over-insurance," 28

partnership, 15, 17, 18, 88, 133-92, 198; "incorporated," 51-2; definition of, 133, general, 134; trading, 134; non-trading, 134; special, 134; limited, 134
policy, five fundamental forms, 28; "corporation form," 30, 69, 75, 83; ordinary life, 30, 60, 69, 74, 83, 91, 139, 149, 175, 180, 187, 204, 218, 233, 239; limited payment life, 30, 83, 91, 139, 204; endowment life, 30, 64, 91, 149, 205, 218; term life, 30, 61, 75, 149, 180, 187, 205, 218 233, 239; modified life, 30, 61, 75, 149, 180, 187, 205, 218, 239
premium payments, 29, 58, 61, 66, 69, 72, 75, 76, 83, 84, 92, 139, 140, 142, 150-1, 158, 175-6, 181, 182, 187, 190, 206, 29, 234, 235, 240, 261
proprietor, 16, 201, 294, 295, 296, 216, 225, 235
proprietorship, 15, 17, 18, 24, 88, 195-243; definition of, 16
protection, amount of, 26, 27; elements of proper, 26-46; amount of for credit reinforcement, 59-60, 138-9; for direct compensation, 68-9, 74, 82-3, 175, 180, 186-7, 238-9; for liquidation fund, 90-1, 148-9; for purchase plan, 217-8
purchase plan, 23, 215-28

questionnaire, 249-54

rating, substandard, 257-60
Revenue Act of 1926, 183

service, physical and medical, 254-57
salesmanship, 8, 9
standard risk, 91
State laws, variation in, 11
State inheritance tax, 41-45, 64, 71, 78, 86, 125, 126, 143, 167, 177, 183, 190, 212, 226, 241, 261
stock purchase plan, 88, 91, 113-4
substandard risk, 28, 128, 257-60

tax, rulings, 41; questions concerning, 42; practices, 43; Federal income, 41-45, 64, 71, 77, 85, 125, 142-3, 167, 177, 183, 190, 212, 226, 235, 241, 261; Federal estate, 41-45, 64, 71, 78, 85, 125, 126, 143, 167, 177, 183, 190, 212, 226, 241, 261; State inheritance, 41-45, 64, 71, 78, 86, 125, 126, 143, 167, 177, 183, 190, 212, 241, 261; Federal

transfer laws, 183, 235; State transfer laws, 183, 235; authorities, 42, 77, 78, 86, 142, 143; exemption, 78
taxation, 41, 46, 64, 71, 77, 85, 125, 142-4, 167-8, 177, 183, 190, 212-3, 226, 235-6, 241-2
teachers, 195
term life insurance, 28, 30, 61, 75, 149, 180, 187, 205, 218, 233, 239
trust, department, 36, 38; officer, 38, 160; companies, 38, 210
trustee, 32, 37-9, 113, 153, 160, 207, 211, 225
trusteeship, 32, 94, 151, 160, 212
trusts, 36, 38, 94, 113, 151, 160, 210, 224-6; expense of, 38

underwriter, life, 9, 11, 34, 40, 41, 52, 53, 64, 147, 180, 204, 221, 235, 239, 247-61
uninsurability, 254

values, cash, 39, 40, 63-4, 71, 77, 85, 124, 141-2, 151, 177, 182, 190, 211, 225, 235, 241

wives as beneficiaries, 31, 93
will, business, 36, 95-6, 98, 198

DATE DUE

GAYLORD			PRINTED IN U.S.A.

HG
8937
.S3
W

000263

Sanborn, Ralph
Business life
insurance.

000263

HG
8937
.S3
W

Sanborn, Ralph
Business life
insurance.

ISSUED TO

HG
8937
.S3
W

000263

Sanborn, Ralph

Business life
insurance.

DR. NORMAN A. WIGGINS

CARRIE RICH MEMORIAL LIBRARY
CAMPBELL COLLEGE
BUIES CREEK, N. C.

Y0-DWG-942